

Graphic Arts and Related Enterprises

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Key to Alternatives:

Agenda C:

1. Mr. Patrick Leone

Agenda D:

1. Graphic Artists Guild
2. Mr. Nicholas Blonder
3. Mr. Don Wayne
4. Mr. Peter Liao
5. American Association of Advertising Agencies (AAAA)

AGENDA A— February 5, 2002 Business Taxes Committee Meeting **Graphic Arts and Related Enterprises - Regulation 1543, Publishers**

<p>Action 1 — Consent Items</p> <p>Agenda A, Pages 2-9.</p>	<p>Adopt proposed amendments for Regulation 1543 as agreed upon by industry and staff.</p>
<p>Action 2 — Authorization to Publish</p>	<p>Recommend the publication of the proposed amendments to Regulation 1543 as adopted in the above actions.</p> <p>Operative Date: None Implementation: 30 days following OAL approval</p>

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Graphic Arts and Related Enterprises - Regulation 1543, Publishers

Action Item	Staff and Industry's Proposed Regulatory Language
Action 1 — Consent Items Exhibit 8	<p>Regulation 1543. PUBLISHERS.</p> <p>(a) DEFINITIONS.</p> <p>—(1) AUTHOR. Author means and includes any person who creates an original manuscript for the purpose of publication. For purposes of this regulation, the following persons are also authors:</p> <p>—(A) Developmental Editors. A developmental editor means and includes any person who consults with an author (as defined above) to develop the concepts in a manuscript or reviews the copy edited manuscript and recommends visual concepts.</p> <p>—(B) Copy Editors. A copy editor means and includes any person who reviews a manuscript for grammatical consistency and clarity.</p> <p>—(C) Manuscript Reviewers. A manuscript reviewer means and includes any person who reviews a manuscript for technical accuracy and acceptability to the proposed audience. For example, a reviewer may review the manuscript of a book on gardening for technical accuracy and suitability of the gardening advice for a particular climate.</p> <p>—(D) Photo researchers. A photo researcher means and includes any person who assists other authors or publishers in obtaining permission and rights from third parties to use photographic images to illustrate a manuscript.</p> <p>—(E) Translators. A translator means and includes any person who produces a manuscript that is a translation of material from a different language.</p> <p>—(2) DESIGNER. Designer means and includes any person who plans and prepares a general layout of typographical and illustrative elements for printed literature.</p> <p>—(3) ART DIRECTOR. Art Director means and includes any person who prepares general specifications (in the form of verbal instructions or rough sketches) for an illustrator or photographer.</p> <p>—(4) PRODUCTION FUNCTION. A production function is a segment of the process of producing camera-ready art or camera-ready copy, and includes but is not limited to the following:</p> <p>—(A) Manuscript Mark-Up: The application of type specifications to a manuscript for typesetting, when done manually.</p> <p>—(B) Formatting: Manuscript mark-up, when done electronically.</p>

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	<p>—(C) Typesetting, Typography or Composition: Composition of type by any method, within the meaning of Revenue and Taxation Code section 6010.3.</p> <p>—(D) Proofreading: A reading of typeset copy for correctness in comparison with the original manuscript.</p> <p>—(E) Alterations: Changes made to typeset copy or camera ready copy.</p> <p>—(F) Dummy: A mock-up or layout of a page showing position and overall form, used for approval. A dummy can be assembled manually or generated by a computer program. A dummy is never incorporated physically into a mechanical or paste up.</p> <p>—(G) Mechanical or Paste-up: Reproduction ("repro") copy, both text and illustrative material, that is ready to be photographed and made into lithographer's film. Also referred to as camera ready art or camera ready copy.</p> <p>—(H) Production Coordination or Production Direction: Coordination and scheduling of the various components of a project.</p> <p>—(I) Production Editing: Maintaining editorial integrity of the author's work during the production process.</p> <p>—(5) PUBLISHER: Publisher means and includes any person who owns the rights to reproduce, market and distribute printed literature.</p> <p>—(6) PRELIMINARY ART: Preliminary art means roughs, visualizations, layouts and comprehensives, title to which does not pass to the client, but which are prepared solely for the purpose of demonstrating an idea or message for acceptance by the client before a contract is entered into or before approval is given for preparation of finished art to be furnished by the seller to his or her client.</p> <p>—(7) FINISHED ART: Finished art means the final art used for actual reproduction by photo mechanical or other processes.</p> <p>—(8) PHOTOSTAT: Photostat means a copy produced by photographic means, often used in layout, dummy work, or "for position only" on camera ready art.</p> <p>—(9) SYNDICATORS: The term syndicator means and includes any person who receives original manuscripts or reproduction proofs thereof, including columns, cartoons, and comic strip drawings, from authors and distributes those manuscripts to publishers for publication.</p> <p><u>(1) ART DIRECTOR.</u> An art director prepares general specifications (in the form of verbal instructions or rough sketches) for an illustrator or photographer.</p> <p><u>(2) AUTHOR.</u> An author creates an original manuscript, whether written by hand, on a typewriter or computer, or otherwise, for the purpose of publication. For purposes of this regulation, the following persons are also authors:</p>

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	<p><u>(A) Copy editor, who reviews a manuscript for grammatical consistency and clarity.</u></p> <p><u>(B) Developmental editor, who consults with the author who created an original manuscript for purposes of publication to develop the concepts in the manuscript, or who reviews the copy edited manuscript and recommends visual concepts.</u></p> <p><u>(C) Manuscript reviewer, who reviews a manuscript for technical accuracy and acceptability to the proposed audience. For example, a reviewer may review the manuscript of a book on gardening for technical accuracy and suitability of the gardening advice for a particular climate.</u></p> <p><u>(D) Photo researcher, who assists other authors or publishers in obtaining permission and rights from third parties to use photographic images for purposes of reproduction in the publication of a manuscript.</u></p> <p><u>(E) Translator, who produces a manuscript that is a translation of material from a different language.</u></p> <p><u>(3) DESIGNER. A designer plans and prepares a general layout of typographical and illustrative elements for printed literature.</u></p> <p><u>(4) FINISHED ART. Finished art is the final artwork used for actual reproduction by photomechanical or other processes, or used for display. It includes electronic art, illustrations (e.g. drawings, diagrams, halftones, or color images), photographic images, sculptures, paintings, and handlettering.</u></p> <p><u>(5) ILLUSTRATOR. An illustrator creates an illustration, which is an original artwork (including cartoons and comic strips) licensed for the purpose of publication.</u></p> <p><u>(6) PHOTOGRAPHER. A photographer creates an original photographic image through the use of a camera or similar device, which photographic image is licensed for the purpose of publication.</u></p> <p><u>(7) PHOTOSTAT. A photostat (also called a "stat") is a copy produced by photographic means, often used in layout, dummy work, or "for position only" on camera-ready art.</u></p> <p><u>(8) PRELIMINARY ART. Preliminary art is tangible personal property which is prepared solely for the purpose of demonstrating an idea or message for acceptance by the client before a contract is entered into or before approval is given for preparation of finished art to be furnished or licensed by the seller to his or her client, provided neither title to nor permanent possession of such tangible personal property passes to the client. Preliminary art may include roughs, visualizations, layouts, comprehensives, and instant photos.</u></p> <p><u>(9) PRODUCTION FUNCTION. A production function is a segment of the process of producing camera-ready art or camera-ready copy, and includes the following:</u></p> <p><u>(A) Alterations, which are changes made to typeset copy or camera-ready copy.</u></p>

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	<p><u>(B) Dummy, which is a mock-up or layout of a page showing position and overall form, used for approval. A dummy can be assembled manually or generated by a computer program. A dummy is never physically incorporated into a mechanical or paste-up.</u></p> <p><u>(C) Formatting, which is a manuscript mark-up, when done electronically.</u></p> <p><u>(D) Manuscript mark-up, which is the application of type specifications to a manuscript for typesetting, when done manually.</u></p> <p><u>(E) Mechanical or paste-up (also called camera-ready art or camera-ready copy), which is produced by preparing copy to make it camera-ready with all type and design elements, and then pasting the prepared copy on artboard or illustration board in exact position along with instructions, either in the margins or on an overlay, for the platemaker.</u></p> <p><u>(F) Production Coordination or Production Direction, which is the coordination and scheduling of the various components of a project.</u></p> <p><u>(G) Production Editing, which is editing that maintains editorial integrity of the author's work during the production process.</u></p> <p><u>(H) Proofreading, which is a reading of typeset copy for correctness in comparison with the original manuscript.</u></p> <p><u>(I) Typesetting, typography, or composition, which is the fabrication or production of composed type, or reproduction proofs thereof, for use in the preparation of printed matter. Typesetting, typography, or composition does not include the fabrication or production of a paste-up, mechanical, or assembly of which a reproduction proof is a component part.</u></p> <p><u>(10) PUBLISHER. A publisher owns, outright or by license, the rights to reproduce, market, and distribute printed literature.</u></p> <p><u>(11) SYNDICATOR. A syndicator receives from authors original manuscripts, or reproduction proofs thereof, including columns, cartoons, and comic strip drawings, and distributes those manuscripts to publishers for publication.</u></p> <p>(b) APPLICATION OF TAX.</p> <p>(1) AUTHORS.</p> <p><u>(A) The transfer by an author to a publisher or syndicator, for the purpose of publication, of an original manuscript or copy thereof, including the transfer of an original column, cartoon, or comic strip drawing, is a service, the charge for which is not subject to sales tax not subject to taxation. Tax does not apply even if the manuscript is transferred in machine-readable form. The transfer of any paper, tape, diskette or other tangible personal property transferred as a means of expressing an idea is not taxable. If the author transfers the original manuscript or copy thereof in tangible form, such as on paper or in machine-readable form such as on tape or compact disc, that transfer is incidental to the author's providing of the service, and the author is the consumer of any such property. However, tax applies to the sale of the transfer of mere copies of an author's work is a sale of tangible personal property, and tax applies accordingly.</u></p>

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	<p>(B) Tax applies to charges for transfers of photographic <u>images</u> and illustrations, whether or not the photographic <u>images</u> or illustrations are copyrighted. Transfers of photographic <u>images</u> or illustrations illustrating text written by the photographer or illustrator are not taxable when they are merely incidental to the editorial matter.</p> <p>(2) SYNDICATORS. The transfer by a syndicator to a publisher of impressed mats or proofs of syndicated columns, cartoons, or comic strip drawings for the purpose of publication is not subject to tax.</p> <p>(3) DESIGNERS AND ART DIRECTORS. Fees paid to a designer or art director for his or her ability to design, conceive, or dictate ideas, concepts, or specifications are not subject to tax if the designer or art director does not transfer to the client or to any other person on behalf of the client title or possession of any tangible personal property used to convey the ideas. The designer or art director is the consumer of any paper, tape, film, diskette, or other tangible personal property used. Tax applies to the sale of such tangible personal property to <u>or use of such tangible personal property by</u> the designer or art director.</p> <p>(4) PRODUCTION FUNCTIONS.</p> <p>(A) Tax applies to the gross receipts from the retail sale of camera-ready art or camera-ready copy. The measure of tax includes charges for the performance of all production functions, whether the charges are separately stated or not.</p> <p>(B) A contract under which a person performs <u>only</u> the following functions <u>(or any combination of the following functions)</u> only is not subject to tax: Mmanuscript mark-up, formatting, typesetting, proofreading, production coordination, and production editing. <u>If Charges for any of such functions are taxable when they are provided as part of the taxable sale of camera-ready copy or camera-ready art unless, are separable in the sense that there is no contract for the camera-ready copy or camera-ready art until after such functions are completed, in which case the charges for such functions are nontaxable.</u></p> <p>(5) CONTRACT TO PERFORM SERVICES AND TO FURNISH TANGIBLE PERSONAL PROPERTY. One person may, under a single agreement, contract both to perform author, design, or art direction services, and to produce camera-ready copy or art. If, under the terms of the agreement, the client retains the right to approve the manuscript, layout, or general specifications before authorizing preparation of camera-ready copy or art, and if the author, designer, or art director does not transfer to the client title to the layouts or possession of the layouts other than for the purpose of review and approval only, then separately stated charges for performance of the services are not taxable. In the absence of specific contractual language, proof of client approval shall be evidenced by contemporaneous notation of receipt of approval in the records of the author, designer, or art director. No other proof shall be required.</p> <p>(6) ILLUSTRATIONSPRELIMINARY ART. Tax does not apply to separately <u>stated</u> charges for preliminary art, except where the preliminary art becomes physically incorporated into the finished art, as, for example, when the finished art is made by inking directly over a pencil sketch or drawing, or the approved layout is used as camera copy for reproduction. The charge for preliminary art <u>is separately stated if it is must be billed separately to the client, either on a separate billing or separately charged for itemized on the billing for the finished art. It must be provided it is clearly identified on the billing as roughs, visualizations, layouts, comprehensives, or other</u></p>

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	<p>preliminary art. Proof of ordering or producing the preliminary art, prior to the date of the contract or approval for finished art, shall be evidenced by purchase orders of the buyer, or by work orders or other records of the seller. No other proof shall be required. Tax applies to the total charges made for finished art. <u>If there is no separately stated charge for preliminary art, then there is no deduction for such services from the taxable measure for the sale of the finished art except as provided in subdivision (b)(2)(C) of Regulation 1540.</u></p> <p>(7) SALES BY PUBLISHERS. Sales of printed literature are subject to tax unless the sale is for resale or is specifically exempted by law, e.g., <u>qualifying</u> sales of printed sales messages and sales in interstate and foreign commerce.</p> <p>(8) <u>TRANSPORTATION CHARGES AND SERVICES RELATED TO TRANSPORTATION.</u> In general, tax applies to charges for the transportation of printed matter in connection with a taxable retail sale except as provided in tangible personal property except under certain conditions. For rules relating to transportation charges, see Regulation 1628, Transportation Charges.</p> <p><u>Separately stated charges for services such as addressing (by hand or by mechanical means), folding, enclosing, or sealing directly related directly to the transportation of printed material matter to the customer are not subject to the tax, e.g., addressing (by hand or by mechanical means), folding, enclosing, or sealing. Tax applies, however, to charges for envelopes except as otherwise provided in Regulation 1541.5.</u></p> <p>(9) PURCHASES OF PROPERTY FOR RESALE. Tax applies to the purchase of tangible personal property that is consumed in any production function and does not become a part of the finished product. However, a person may purchase such property for resale if <u>that person's contract of sale with its client explicitly passes</u> title to the property passes to that person's client prior to its use. Tangible personal property so purchased must be separately listed and priced on the person's sales invoice to the client and sales tax charged when appropriate and sales tax applies to that charge. Art work is considered to be used if it is photocopied. If artwork is purchased together with a photostat of the artwork and the purchaser uses only the photostat but not the artwork, the artwork may be purchased for resale. Tax applies to the charge made for the photostat.</p> <p><u>(10) REPRODUCTION RIGHTS. Notwithstanding anything to the contrary in this regulation, if the transfer of a photographic image or artwork is made pursuant to a technology transfer agreement under subdivision (b)(2)(D)2. of Regulation 1540, tax applies to the transfer of the artwork in accordance with that provision.</u></p> <p>(c) EXAMPLES OF THE APPLICATION OF TAX UNDER SPECIFIC CIRCUMSTANCES.</p> <p>(1) A firm provides various services to a publisher. In performing a contract with the publisher, the firm buys a color separation from a third party. The firm does not make a copy of the color separation or use it in any way, but resells it to the publisher. The firm may give a resale certificate to the third party but tax applies to the sale to the publisher.</p> <p>(2) The firm in Example (1) uses the color separation before reselling it to the publisher. Both the firm and the publisher are consumers, and both sales are subject to tax.</p>

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	<p>(3) The firm in Example (1) buys both the color separation and a photostatic copy (“stat”) of it from the third party who separately states the price of each item on his <u>the sales</u> invoice. The firm retains the stat photostatic copy but resells the color separation to the publisher without using it in any way. <u>Since the third party used the color separation to make a copy of it, the sale of the component parts to the third party, or the third party's use of those component parts, is subject to tax.</u> The firm may give a resale certificate to the third party for the color separation, but tax applies to the third party's sale of the stat photostatic copy. Tax also applies to the firm's sale of the color separation to the publisher.</p> <p>(4) A firm contracts with a publisher to perform a contract in three stages, as follows:</p> <p>(A) The firm creates an original manuscript of a book. The publisher reviews the first draft, comments on it, and approves it. The firm then does developmental editing, in which the writer and editors develop the manuscript for sound editorial structure and organization. The publisher reviews the resulting second draft, comments on it, and approves it. The firm then does copy editing, in which editors review the manuscript for grammatical consistency and clarity. After this, the firm passes title to the manuscript to the publisher for the purpose of publication. Under the contract, the firm can proceed with further work only with the publisher's approval.</p> <p>Tax does not apply to the sale of the finished manuscript or to any of the steps of writing and editing it.</p> <p>(B) In the second stage, the publisher returns the accepted manuscript to the firm for typesetting into galleys, which the publisher reviews and approves. The firm then arranges the galleys into page form, which the publisher reviews and approves. The firm then produces camera-ready art, which the publisher reviews for approval or alterations. The publisher then accepts and takes title to the camera-ready art.</p> <p>Tax applies to the firm's gross receipts from the sale of the camera-ready art, including formatting, typesetting, proofreading, and production coordination, whether separately stated or not. To preserve the exempt nontaxable status of the receipts described in Example (4)(A), above, <u>the receipts charges for work done in Example (4)(A) should must be separately stated from the receipts charges for the sale of the tangible personal property in this Example (4)(B).</u></p> <p>(C) In the third stage, the publisher returns the camera-ready art to the firm for printing. The firm subcontracts the printing to a printer. The firm manages the quality of the printing. A representative of the publisher visits the printer to approve the work. At the firm's instruction, the printer ships the completed books to the publisher's warehouse.</p> <p>The <u>Since the firm will be reselling the books to the publisher without using them, the firm may issue a resale certificate to the printer. Since the publisher intends to resell the books, the publisher may furnish issue a resale certificate to the firm, who may in turn furnish a resale certificate to the printer (provided the firm does not use the completed books in any way).</u> Tax applies to sales <u>of the books</u> by the publisher to consumers <u>unless the sales are specifically exempt by statute (e.g., sales in interstate commerce).</u></p> <p>(5) A publisher owns an existing manuscript. The publisher contracts with an editorial design firm for developmental editing, copy editing, and design specifications. The firm reviews the manuscript and makes recommendations to the publisher for developing it into</p>

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	<p>publishable form, including recommended layout and a general approach to design (e.g., trim size). After the publisher accepts these recommendations, a designer (at the firm or a subcontractor) prepares sample sketches and dummies to express the idea to the publisher. After the publisher approves the sketches and dummies, the designer creates type specifications. A developmental editor and a copy editor (at the firm or a subcontractor) perform development and copy editing services. The edited manuscript, dummies, and type specifications are transferred to the publisher.</p> <p>Tax does not apply to the editing services because they are author's services. Tax does not apply to <u>charges for the dummies and type specifications</u> if the charges for the dummies and type specifications <u>those charges</u> are separately stated and if possession and title is retained by the editorial design firm.</p> <p>(6) A publisher has an office in California and an office in New York. The publisher's California office purchases camera-ready art from a California production firm with title passing in California. However, the production firm, on instructions from the publisher, ships the camera-ready art directly to the publisher's New York office <u>for use at the New York office, with no use of the camera-ready art in California.</u></p> <p>Tax does not apply to the production firm's gross receipts from the sale of the camera-ready art, because the sale is in interstate commerce.</p> <p><u>(7) A commercial artist (such as a commercial photographer or illustrator) makes a temporary transfer of finished art (such as a photograph or illustration) that qualifies as a technology transfer agreement under subdivision (b)(2)(D)2. of Regulation 1540 to a publisher for purposes of reproducing the finished art in a children's book. The publisher makes a computer scan of the finished art and returns the original finished art to the commercial artist. The publisher incorporates the computer scan into layouts which are used to reproduce the finished art in the printed children's books, which are then sold. The commercial artist is paid an advance against royalties, and is then paid royalties based on retail sales of the children's book. The commercial artist does not make a separate charge for the tangible personal property leased to the publisher in accordance with subdivision (b)(2)(D)2.a. of Regulation 1540. As provided in subdivision (b)(2)(D)2.b. of Regulation 1540, if the commercial artist has leased like property for a separate price to an unrelated third party without also transferring an interest in the copyright, or has leased that finished art or like finished art for a separate price satisfying the requirements of subdivision (b)(2)(D)2.a. of Regulation 1540, then tax applies to that separate price. Otherwise, tax applies to the commercial artist's transfer as specified in subdivision (b)(2)(D)2.c. of Regulation 1540. Except for the tax due under subdivision (b)(2)(D)2.b. or (b)(2)(D)2.c. of Regulation 1540, no further tax is due on the royalties or the advance paid to the commercial artist. Tax applies to the retail sales of the children's book unless specifically exempt by statute.</u></p>

**AGENDA B— February 5, 2002 Business Taxes Committee Meeting
Graphic Arts and Related Enterprises - Regulation 1528, Photographers,
Photocopiers, Photo Finishers and X-Ray Laboratories**

<p>Action 1 — Consent Items</p> <p>Agenda B, Pages 2-5.</p>	<p>Adopt proposed amendments for Regulation 1528 as agreed upon by industry and staff.</p>
<p>Action 2 — Authorization to Publish</p>	<p>Recommend the publication of the proposed amendments to Regulation 1528 as adopted in the above actions.</p> <p>Operative Date: None Implementation: 30 days following OAL approval</p>

AGENDA B— February 5, 2002 Business Taxes Committee Meeting
Graphic Arts and Related Enterprises - Regulation 1528, Photographers, Photocopiers,
Photo Finishers and X-Ray Laboratories

Action Item	Staff and Industry's Proposed Regulatory Language
<p>Action 1 — Consent Items Exhibit 9</p>	<p>Regulation 1528. PHOTOGRAPHERS, PHOTOCOPIERS, PHOTO FINISHERS AND X-RAY LABORATORIES.</p> <p>Reference: Sections 6006, 6009, 6015, and 6020, Revenue and Taxation Code.</p> <p>(a) PHOTOGRAPHERS AND PHOTOCOPIERS. Tax applies to sales of photographs, whether or not produced to the special order of the customer. Tax applies to sales of photocopies, whether or not produced to the special order of the customer, and to charges for the making of photographs or photocopies out of materials furnished by the customer or others. Except as provided in subdivision (b)(2), no deduction is allowable on account of expenses such as travel time, telephone calls, rental of equipment, or salaries or wages paid to assistants or models, whether or not such expenses are itemized in billings to customers.</p> <p>Tax does not apply to sales to photographers and persons who make photocopies of tangible personal property which becomes an ingredient or component part of photographs or photocopies sold, such as mounts, frames, sensitized paper, and toner but does apply to sales to the photographer or producer of materials used in the process of making the photographs or photocopies and not becoming an ingredient or component part thereof, such as chemicals, trays, films, plates, proof paper, cameras, and copy machine drums.</p> <p><u>See Regulation 1540, <i>Advertising Agencies and Commercial Artists</i>, for transfers of photographic images by commercial artists.</u></p> <p>(b) PHOTOCOPYING OF RECORDS.</p> <p>(1) GENERAL RULES. Tax applies to sales of photocopies of records. Persons who make and sell, or obtain and sell, photocopies of records to consumers are retailers of the photocopies whether they make the photocopies themselves, hire a subcontractor to make the photocopies, or acquire the photocopies for resale from the person who owns or maintains the records. Tax applies whether or not the copies are made at the business location of the retailer or at the location of the person who owns or maintains the records. The tax applies to the entire charge for making and selling, or obtaining and selling, photocopies, without deduction for expenses incurred in obtaining access to the records, travel time, time spent in</p>

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Photo Finishers and X-Ray Laboratories

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	<p>selecting the particular records desired, the field service of photocopying or microfilming the records, telephone calls, file setup charges, basic fees, typing fees, document handling fees, or any other costs or expenses of filling the customer's order.</p> <p>(2) SERVICE TRANSACTIONS. Merely because a fee is charged in connection with the transfer of a photocopy of a record does not mean that the transaction is a sale transaction under the Sales and Use Tax Law. If a person who owns or maintains the records (recordholder) is required by law to furnish the photocopy upon tender and payment of a fee, the transfer of the photocopies by that person is not a sale. For sales and use tax purposes, that person is the consumer of the photocopies transferred and charges by a photocopy company to the recordholder for the photocopies are subject to tax.</p> <p>(A) Medical Records. Ordinarily tax does not apply to charges made by a hospital or other health care provider (recordholder) for photocopying of medical records. The transaction is regarded as a service transaction, and the fees are nontaxable if the photocopies are furnished to the patient, or to someone acting on behalf of the patient, or to the patient's representative as provided in Health and Safety Code section 123110(b). Likewise, the fees are nontaxable if the photocopies are furnished in response to a written authorization presented by an attorney or the attorney's representative as provided in Evidence Code section 1158, or if the photocopies are furnished as provided in subdivision (b)(2)(C) below. Tax does apply, however, if the hospital or other health care provider is not required by law to furnish photocopies but otherwise sells photocopies of records for a price. Charges made by a photocopy company directly to the requesting party for photocopies which, by agreement with the recordholder, were made and furnished directly to the requesting party are taxable in their entirety.</p> <p>The preparation and service of a written authorization as provided in California Evidence Code Section 1158 is a nontaxable service. The tax does not apply to separately stated charges for this service even though the written authorization is served in connection with the performance of a contract to produce and deliver photocopies of records.</p> <p>(B) Public Records. Tax does not apply to charges made by a public agency for photocopies of records furnished pursuant to the California Public Records Act or local law, ordinance, or resolution. Persons who obtain photocopies of public records from public agencies and sell the photocopies are making retail sales and must pay sales tax measured by their entire charge, including reimbursement of legally required fees.</p> <p>(C) Witness Fees. Copying, witness, mileage or other fees which are charged by a person who furnishes copies of records in response to a subpoena as provided in California Evidence Code Section 1563 are not subject to tax. Separately stated charges by a photocopy company for the reimbursement of witness fees which were paid to the recordholder are not subject to tax. Tax does not apply to separately stated fees, made by a person who makes or acquires records for another for</p>

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	<p>advancing payment of statutory witness fees. Such fees, commonly identified as “check charges”, are made to cover the cost of providing the check, advancing moneys, and associated bookkeeping costs. When a witness fee is charged, the “check charge” will be regarded as part of the charge for a nontaxable service and not as a part of the charge made for the tangible personal property.</p> <p>(3) PREPARATION OF SUBPOENA DUCES TECUM. The preparation and service of a subpoena duces tecum is a nontaxable service. The tax does not apply to separately stated charges made for the service even though the subpoena is served in connection with the performance of a contract to produce and deliver photocopies of records.</p> <p>(4) TYPEWRITTEN TRANSCRIPTIONS AND INTERPRETATION OF MEDICAL RECORDS. The tax does not apply to a separately stated charge made for providing a typewritten transcription of a medical report or an interpretation of the contents of a medical record. However, the tax applies to the fair retail value of any photocopies produced for the customer in connection with the nontaxable service.</p> <p>(c) PHOTO FINISHERS.</p> <p>(1) PRINTS AND ENLARGEMENTS. Tax applies to charges for printing pictures or making enlargements from negatives or slides furnished by the customer.</p> <p>Tax applies to sales to photo finishers of all tangible personal property used by them in printing pictures or making enlargements except property becoming an ingredient or component part of the prints, enlargements and other items sold by them.</p> <p>(2) COLORING AND TINTING. Tax applies to charges for coloring and tinting new pictures.</p> <p>Tax does not apply to sales of colors and tints to photo finishers for use by them in coloring and tinting new pictures.</p> <p>(3) FILM PROCESSING.</p> <p>(A) Negative Development of Customer Furnished Film. Tax does not apply to separately stated charges for the negative development of customer furnished film. Development of film by the reverse process method is not the negative development of film.</p>

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	<p>Tax applies to sales of chemicals for use in such negative development whether or not the chemicals become a component part of the negative.</p> <p>(B) Other Film Processing. Tax applies to all film processing charges other than separately stated charges for the negative development of customer furnished film. For example, tax applies to charges for development of film by the reverse process method.</p> <p>Tax applies to sales of chemicals for use in such film processing if the chemicals do not become a component part of the processed film transferred to customers. Tax does not apply to sales of chemicals which do become a component part of film sold to customers before use.</p> <p>(d) X-RAY LABORATORIES. Producers of X-Ray films or photographs for the purpose of diagnosing medical or dental conditions of humans, excluding such films and photographs used only for cosmetic purposes, are the consumers of materials and supplies used in the production thereof. Thus, the tax applies to the sale of such materials and supplies to laboratories producing X-Ray films or photographs for the purpose of such diagnoses. Whether the laboratory is a "lay laboratory" or is operated by a physician, surgeon, dentist or hospital is immaterial. Producers of X-Ray films or photographs for any other purpose such as use for purely cosmetic purposes, diagnosis of medical or dental conditions of animals, inspection of metals, welds and similar purposes are retailers of the films or pictures and the tax applies to the gross receipts from the retail sale thereof. If, however, an X-Ray laboratory contracts to furnish an X-Ray inspection service, retaining title to and possession of the X-Ray or pictures produced, charges for the performance of such an inspection service are not subject to tax.</p>

AGENDA C — February 5, 2002 Business Taxes Committee Meeting
Graphic Arts and Related Enterprises - Regulation 1541, Printing and Related Arts

<p>Action 1 — Consent Items</p> <p>Agenda C, Pages 2-9.</p>	<p>Adopt proposed amendments to Regulation 1541 as agreed upon by industry and staff.</p>
<p>Action 2 — Special Printing Aids</p> <p>Subdivision (c)</p> <p>Agenda C, Pages 10-26.</p>	<p>Adopt either:</p> <ol style="list-style-type: none"> 1) Staff’s recommendation to replace the confusing terminology of “ultimately subject to sales tax” with a clear explanation of the application of tax in subdivision (c); OR 2) Mr. Patrick Leone’s proposal to not replace the terminology “ultimately subject to sales tax” and leave subdivision (c) unchanged; OR 3) If staff’s recommendation is adopted, Mr. Leone proposes that the change be applied on a prospective basis in subdivisions (c)(2)(B) and (c)(2)(B)1.
<p>Action 3 — Authorization to Publish</p> <p>(whichever language is approved)</p>	<p>Recommend the publication of the proposed amendments to Regulation 1541 as adopted in the above actions.</p> <p>Operative Date: As adopted in Action 2 Implementation: 30 days following OAL approval</p>

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Graphic Arts and Related Enterprises - Regulation 1541, Printing and Related Arts

Action Item	Staff and Industry's Proposed Regulatory Language
Action 1 — Consent Items	<p>Regulation 1541. PRINTING AND RELATED ARTS.</p> <p><i>Reference:</i> <input type="checkbox"/> Sections 6006-6012, Revenue and Taxation Code.</p> <p><u>(a) DEFINITIONS.</u></p> <p>—(1) SPECIAL PRINTING AID. The term “special printing aid” means a reusable manufacturing aid which is used by a printer during the printing process and is of unique utility to a particular customer. Examples of special printing aids include, but are not limited to, electrotypes, stereotypes, photoengravings, silk screens, steel dies, cutting dies, lithographic plates, artwork, film, single color, or multicolor separation negatives, and flats.</p> <p>—(2) PRINTING PROCESS. The term “printing process” includes, but is not limited to, letterpress, flexography, gravure, offset lithography, reprography, screen printing, steel die engraving, thermography, laser, inkjet, and photocopying.</p> <p>—(3) REPRODUCTION PROOF. A direct impression of composed type forms containing type matter only or type matter combined with clip art, or a copy of that direct impression made by any method including the diffusion transfer method, and used exclusively for reproduction.</p> <p>—(4) MECHANICAL OR PASTE UP. Preparation of copy to make it camera ready with all type and design elements pasted on artboard or illustration board in exact position and containing instructions, either in the margins or on an overlay, for the platemaker. Also referred to as camera-ready art or camera-ready copy.</p> <p>—(5) CLIP ART. Prepackaged art (including photographic images), not produced to the special order of the customer, commercially available on CD Rom, other electronic media or by computer program for use in digital page layout. Images that are enlarged, reduced or rotated are not considered “produced to the special order of the customer.” When distributed in digital form, clip art is often referred to as “click art”.</p> <p><u>(1) CLIP ART. Clip art is prepackaged art (including photographic images) which is not produced to the special order of the customer and which is commercially available on CD ROM, other electronic media, or by computer program for use in digital page layout. Images that are enlarged, reduced, or rotated are not considered “produced to the special order of the customer.”</u></p> <p><u>(2) COLOR SEPARATOR. A color separator is a person who engages in the process of color separation. The process of color separation divides a full color photographic image into four separate components, corresponding to the four primary colors used in process color printing. The color separator may accomplish this photographically or electronically, and the products of this process may be either a negative or positive film separation or a separated printing plate.</u></p>

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	<p><u>(3) COLOR SEPARATION WORKING PRODUCTS.</u> Color separation working products consist of property such as photographic film for making transparencies, masks, internegatives, interpositives, halftone negatives, composite color separation negatives, goldenrod paper and mylar plastic used in making flats, tape used in stripping negatives into flats, developing chemicals which become a component part of negatives and positives, proofing material and ink used in making final proofs, progressive proofs, and similar items, which are similar in function to special printing aids as defined in subdivision (a)(12).</p> <p><u>(4) DIGITAL PRE-PRESS INSTRUCTION.</u> Digital pre-press instruction is the creation of original information in electronic form by combining more than one computer program into specific instructions or information necessary to prepare and link files for electronic transmission for output to film, plate, or direct to press, which is then transferred on electronic media such as tape or compact disc.</p> <p><u>(5) FINISHED ART.</u> Finished art is the final artwork used for actual reproduction by photomechanical or other processes, or used for display. It includes electronic artwork, illustrations (e.g. drawings, diagrams, halftones, or color images), photographic images, sculptures, paintings, and handlettering.</p> <p><u>(6) INTERMEDIATE PRODUCTION AIDS.</u> Intermediate production aids include items such as artwork, illustrations, photographic images, photo engravings, and other similar materials which are used to produce special printing aids or other intermediate production aids.</p> <p><u>(7) MECHANICAL OR PASTE-UP.</u> A mechanical or paste-up (also called camera-ready art or camera-ready copy) is produced by preparing copy to make it camera-ready with all type and design elements, and then pasting the prepared copy on artboard or illustration board in exact position along with instructions, either in the margins or on an overlay, for the platemaker.</p> <p><u>(8) PRINT BROKER.</u> A print broker is a person who contracts to sell printed matter, but who does not actually engage in the printing process to produce the printed matter to be sold, instead purchasing the printed matter from a printer or from another print broker for resale to the print broker's customer. A person who sells printed matter for which that person did not engage in the printing process is acting as a print broker even if that person engages in the print process for other contracts.</p> <p><u>(9) PRINTER.</u> A printer is a person engaged in the printing process.</p> <p><u>(10) PRINTING PROCESS.</u> The printing process involves activities related to the production of printed matter such as letterpress, flexography, gravure, offset lithography, reprography, screen printing, steel-die engraving, thermography, laser printing, inkjet printing, and photocopying.</p> <p><u>(11) REPRODUCTION PROOF.</u> A reproduction proof is used exclusively for reproduction. It consists of either a direct impression of composed type forms containing type matter only or type matter combined with clip art, or a copy of that direct impression made by</p>

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	<p><u>any method, including the diffusion transfer method.</u></p> <p><u>(12) SPECIAL PRINTING AIDS. Special printing aids are reusable manufacturing aids which are used by a printer during the printing process and are of unique utility to a particular customer. Special printing aids include electrotypes, stereotypes, photoengravings, silk screens, steel dies, cutting dies, lithographic plates, film, single color or multicolor separation negatives, and flats. For purposes of this regulation, special printing aids includes items defined by subdivision (a)(6) as intermediate production aids.</u></p> <p>(b) APPLICATION OF TAX.</p> <p><u>(1) SALES BY PRINTERS. Tax applies to charges for printing of tangible personal property for consumers, regardless of whether or not the paper and other materials are furnished by the consumer. The production of printed matter for a consumer is a sale of tangible personal property whether the materials incorporated into the printed matter are furnished by the consumer or the printer. Unless that sale is exempt from tax, the measure of tax is tax applies to the total gross receipts or sales price of the sale with no deduction on account of: (a) the cost of the raw materials or other components; (b) labor or service costs of any step in the process of producing, fabricating, processing, printing, or imprinting the tangible personal property; or (c) any other expenses or services that are a part of the sale. Services that are a part of the sale of tangible personal property to consumers include, but are not limited to charges for overtime, set-up, die cutting, embossing, folding (except as provided in subdivision (h)(g) below), and other binding operations. Printers may not deduct from the gross receipts or sales price from of their sales of printed matter charges related to their typography work or the cost of typography or typesetting to them, nor can they deduct the costs of special printing aids for which they are consumers under subdivision (c)(1)(A), whether or not a separate charge is made to the customer for the special printing aids. Receipts attributable to such costs are includable in the measure of tax.</u></p> <p>Tax applies to a printer's sale of special printing aids as provided in subdivision (c).</p> <p><u>(2) PURCHASES BY PRINTERS. Printers are consumers of tangible personal property which is not sold prior to use or physically incorporated into the article to be sold. Tax applies to the sale of such property to, or to the use of the property by, the a printer and also to any sale subsequent to its use by the printer. Such property includes, but is not limited to, Property ordinarily consumed by a printer includes machinery (e.g., printing presses, cameras, electronic ——— digital pre-press equipment, and plate makers), office equipment, and printing aids. Printers, however, may purchase special printing aids for resale as explained in subdivision (c).</u></p> <p>(e) SPECIAL PRINTING AIDS. In General. <u>In recognition of the unique utility that special printing aids have to the sale of printed material, and the need to avoid burdening businesses with unnecessary paperwork, the following presumptions shall apply:</u></p> <p><u>—(1) With respect to sales of printed material ultimately subject to sales tax, or sales to the U. S. Government, it shall be presumed that the selling price of the printed material includes the selling price of the special printing aids and that title passed to the customer, irrespective of whether or not the printer separately itemizes the special printing aids. It shall be further presumed that the printer, or other reseller, discussed in the following paragraph, made no use of the special printing aids prior to their sale. Accordingly the printer</u></p>

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	<p>may purchase the special printing aids for resale.</p> <p>“Ultimately subject to sales tax,” means either the printer's sale of the printed material and special printing aids is subject to sales tax or is an exempt sale to the U. S. Government, or if the printer's sale of the printed material is for resale, a subsequent sale of the printed material and special printing aids is subject to California sales tax or is an exempt sale to the U. S. Government.</p> <p>When the printer's sale of printed material is a sale for resale, as described in the above paragraph, unless the printer timely takes a valid resale certificate in good faith that states the special printing aids are to be purchased for resale, tax is due on the selling price of the special printing aids whether or not the selling price is separately itemized. The selling price of the special printing aids is deemed to be the sales price of the special printing aids, or their components, to the printer regardless of the amount of the separately stated charge, if any, for the special printing aid. The printer need not separately charge sales tax reimbursement to their customer and if the printer has paid sales or use tax on the selling price of the special printing aids or their components to the printer, no additional tax is due.</p> <p>The term “special printing aids” on a resale certificate shall be sufficient to cover all special printing aids as defined in subdivision (a)(1).</p> <p>–(2) If a printer does not wish to sell special printing aids in connection with the sale of printed material ultimately subject to sales tax or sold to the U. S. Government, described in (c)(1) above, the following statement should be included on the sales invoice: “The selling price of the printed material does not include the transfer of title to the special printing aids.” The printer would then be the owner and consumer of the special printing aids. Tax would apply to both the retail sale of the printed material and the cost to the printer of the special printing aids.</p> <p>–(3) With respect to all other sales of printed material, as for example, sales in interstate commerce, sales of exempt newspapers or periodicals, or sales of exempt printed sales messages, it shall also be presumed that the selling price of the printed material includes the selling price of the special printing aids and that title passed to the customer irrespective of whether or not the printer separately itemizes the special printing aids. It shall be further presumed that the printer made no use of the special printing aids prior to their sale. Sales tax is due on the selling price of the special printing aids whether or not the selling price of the special printing aids is separately stated. The selling price of the special printing aids is deemed to be the sales price of the special printing aids, or their components, to the printer regardless of the amount of the separately stated charge, if any, for the special printing aid.</p> <p>The printer need not separately charge sales tax reimbursement to their customer and if the printer has paid sales or use tax on the selling price of the special printing aids or their components to the printer, no additional tax is due.</p> <p>However, sales tax is not due on the selling price of the special printing aids discussed in (c)(3) if the printer timely takes a valid resale certificate in good faith that states the special printing aids are to be purchased for resale. The term “special printing aids” on a resale certificate shall be sufficient to cover all special printing aids as defined in subdivision (a)(1).</p>

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	<p>Persons issuing resale certificates for special printing aids as discussed in (c)(3) are then liable for the tax on their selling price of the special printing aids irrespective of whether or not the printer separately itemized the printing aids to the person issuing the resale certificate and notwithstanding that the printed material is exempt from tax as for example, a sale in interstate commerce, a sale of exempt newspapers or periodicals or a sale of exempt printed sales messages. In no event shall the selling price of the special printing aids be less than the selling price of the special printing aids, or their components, to the printer.</p> <p>If the printer's sale includes both a sale of printed material ultimately subject to sales tax, as described in (c)(1) above, and a sale of printed material as described in (c)(3) ("split sale"), tax is due on the selling price of the special printing aids. Absent a separate itemization, as long as tax is reported on an amount equal to at least the selling price of the special printing aids or their components to the printer, no further tax will be due on the selling price of the special printing aids.</p> <p>(4) If a printer does not wish to sell special printing aids in connection with all other sales of printed material, as discussed in (c)(3) above, the following statement should be included on the sales invoice: "The selling price of the printed material does not include the transfer of title to the special printing aids." The printer would then be the owner and consumer of the special printing aids. Tax would apply to the cost to the printer of the special printing aids.</p> <p>(5) No other proof shall be required with respect to passage of title on special printing aids.</p> <p><u>(d) CONCEPTUAL SERVICES.</u></p> <p><u>(1) When the printer makes a lump sum charge for a taxable sale of printed matter, the full lump sum charge is subject to tax with no deduction on account of any conceptual or other services performed to produce that printed matter. When the printer itemizes its charges for a taxable sale of printed matter, tax applies to the printer's entire charge except as provided below.</u></p> <p><u>(2) As part of its contract to produce and sell printed matter, a printer may also agree to acquire finished art for use in producing the printed matter, and the acquisition of that finished art may involve the providing of services to convey ideas, concepts, looks, or messages to a printer's customer which result in a transfer, enhancement, or revision of either electronic artwork, hard copies of electronic artwork, or copies of manually prepared artwork. If the printer states a separate charge for such services which are itemized as "design charges," "preliminary art," "concept development," or any other designation that clearly indicates that the charges are for such services and not for finished art, they are nontaxable unless the contract of sale provides that the printer will pass to its customer title or the right to permanent possession of the artwork in tangible form, such as on electronic media or hard copy, or permanent possession of the artwork in tangible form is, in fact, transferred to the client. The remainder of the printer's charge is subject to tax.</u></p> <p><u>(3) If a printer separately itemizes charges for finished art that also include charges for conceptual services described in subdivision (d)(2), it will be rebuttably presumed that 75 percent of the combined charge for the finished art and conceptual services is for the</u></p>

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	<p><u>nontaxable services. If, however, the printer acquires the finished art and conceptual services from a commercial artist (rather than producing the finished art itself) and the commercial artist itemizes a separate charge for conceptual services that is less than 75 percent of the commercial artist's combined charge for conceptual services and finished art, that lesser percentage shall be applied to the printer's combined charge for final art and conceptual services to determine the total nontaxable charges for conceptual services. Tax applies to the remaining portion of the combined charge for final art and conceptual services unless: 1) the printer passes title to the final art to its customer; and 2) that transfer qualifies a technology transfer agreement under subdivision (b)(2)(D)2 of Regulation 1540, in which case tax applies to the charge for finished art in accordance with that provision. A separately itemized charge for special printing aids is not a separately itemized charge for finished art and conceptual services, and no portion of that charge is excluded from tax as a charge for nontaxable conceptual services.</u></p> <p>(d)(e) COLOR SEPARATORS. The application of tax to printers as explained in <u>this regulation subdivisions (b) and (c)</u> also applies to color separators. Color separators are consumers and not retailers of tangible personal property which is not sold prior to use or physically incorporated into the article to be sold. Tax applies to the sale of such property to <u>or to the use of such property by</u> the color separator. <u>Examples of such property include, but are not limited to, filters and screens, trial proofing materials, disposable lithographic plates, and developing chemicals which do not become incorporated into the article sold. Color separator working products are special printing aids for purposes of this regulation, and the provisions of subdivision (c) apply to their purchase and sale. Color separators, and persons such as printers when acting as color separators, or printers may purchase property such as photographic film for making transparencies, masks, internegatives, interpositives, halftone negatives, composites color separation negatives, goldenrod paper and mylar plastic used in making flats, scotch tape used in stripping negatives into flats, developing chemicals which become a component part of negatives and positives, proofing material and ink used in making final proofs, progressive proofs, and similar items, which are similar in function to special printing aids as defined in subdivision (a)(8) (a)(1), all commonly referred to as "color separator working products" for resale when title to such property passes to the customer prior to use by the color separator or the printer as described in subdivision (c). The term "color separator working products" or "special printing aids" on a resale certificate shall be sufficient to cover all such products.</u></p> <p>Charges for alterations of film work for \$100 or less shall be considered charges for restoring property to its original condition and not subject to tax. Charges greater than \$100 shall be considered charges for fabrication labor and subject to tax.</p> <p>(e)(f) COMPOSED TYPE.</p> <p>(1) IN GENERAL. Tax does not apply to the fabrication or transfer by a typographer or typesetter of composed type, or reproduction proofs of such composed type to printers to use in the preparation of printed matter. The composition of type is the performance of a service, and tax does not apply to charges for such service, unless that service is a part of the sale of printed matter. Tax applies to the gross receipts from the sale of printed matter without any deduction for the charge for typography. <u>Tax applies See subdivision (e)(3) below for the application of tax to charges for transfers of composed type combined with artwork as provided in subdivision (f)(3).</u></p>

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	<p>Typographers and typesetters are the consumers and not retailers of materials, such as typesetting machinery, metal forms, galleys, proofing paper, and cleaners which are used in the performance of their service and are consumers of materials transferred to their customers incidental to the performance of nontaxable typography or typesetting services, such as clip art that is combined with text on the same page.</p> <p>Composed type includes type together with lined borders and plain, straight, fancy, or curved lines. Composed type also includes charts, tables, graphs, and similar methods of providing information.</p> <p>(2) PHOTOCOMPOSITION (INCLUDING PHOTOTYPESETTING AND COMPUTER TYPESETTING). Tax does not apply to the composing of type regardless of whether the type is composed by means of such simplified methods as standard typewriter, desktop publishing, Varsity or Justwriter; by means of photolettering or headlining machines; or by means of a photocomposition (including computer photocomposition) method. Tax does not apply to the transfer, whether temporary or permanent, of the direct product of the type composition service or copy thereof (e.g., typeset matter direct from the typesetting machine ready to be cut and pasted up for reproduction or computer generated type), if that product contains text only or text combined with clip art, whether that product is a paper or film (negative or positive) product, provided the product or copy is to be used exclusively for reproduction.</p> <p>The transfer of camera-ready copy containing text only or text and clip art in the form of a paste-up, mechanical, or assembly, or a camera-ready reproduction of such, is the transfer of composed type and the charge made by the typographer or typesetter to his or her customer is not subject to tax. Tax does not apply to the transfer of a direct photoreproduction of type composed by means of a photolettering or headlining machine or other similar device.</p> <p>Camera-ready copy which is produced through the use of desktop publishing software and a personal computer is nontaxable composed type provided it does not contain artwork other than clip art.</p> <p>Transfers of plates and mats for use in the printing process which are produced using composed type are subject to tax, and tax applies to the entire charge made to the customer including any portion of the charge attributable to the type composition service, whether that charge is separately stated or not. Transfers of engraved printing plates and duplicate plates such as electrotypes, plastic plates, rubber plates, and other plates used in letterpress printing are subject to tax. Similarly, transfers of exposed presensitized, wipe-on, deep-etch, bi-metal and other plates used in offset lithography or of exposed plates produced by a photo-direct method, do not qualify as transfers of reproduction proofs of composed type and are subject to tax. A transfer of gelatin coated film to be transferred to fine mesh silk in the silk-screening process is subject to tax.</p> <p>(3) ARTWORK. Artwork, other than clip art combined with composed type on the same page, is not composed type. The term "artwork" includes, but is not limited to, illustrations (e.g., drawings, diagrams, halftones, or color images), photographic images, drawings, paintings, handlettering, and computer generated artwork. If the basis for billing is on a per page basis, the charge for any page with artwork is subject to sales tax and the charge for any page with only text, or text and clip art, is not subject to tax. If the basis for billing is lump sum, the ratio of pages containing artwork to the total number of pages, applied to the lump sum charge,</p>

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	<p>represents the retail selling-sale price of the artwork and is subject to tax, but in no event shall the retail selling-sale price of the artwork be less than the selling-sale price of the artwork, or its components, to the typographer.</p> <p>However, if the ratio computed above is 10% or less <u>ten percent or fewer of the pages contain artwork</u>, the true object of the sale shall be deemed to be a sale of typography services <u>with an incidental transfer of artwork</u>, and the typographer is the consumer of the that artwork. Tax applies to the selling-sale price of the artwork, or its components, to the typographer. Tax does not apply to the sale of the typography service as explained in (e)(1) <u>subdivision (f)(1)</u>.</p> <p><u>(4) REPRODUCTION RIGHTS.</u> Notwithstanding subdivision (f)(3), if the transfer of artwork qualifies as a technology transfer agreement under subdivision (b)(2)(D)2. of Regulation 1540, tax applies to the transfer of the artwork in accordance with that <u>provision</u>.</p> <p><u>(f)(g) TRANSFERS OF INFORMATION ON COMPUTER DISK OR OTHER ELECTRONIC MEDIA-DIGITAL PRE-PRESS INSTRUCTION.</u></p> <p>The transfer by the seller of the original information created by combining more than one computer program into specific instructions or information necessary to prepare and link files for electronic transmission for output to film, plate, or direct to press, is not subject to tax when transferred by computer disk or other electronic storage media and the original information is a custom computer program. Such a process, currently termed "electronic or digital pre press instruction," creates a new program which shall be considered <u>Digital pre-press instruction</u> is a custom computer program as defined under section 6010.9 of the Revenue and Taxation Code, <u>the sale of which and</u> is not subject to tax, <u>provided if the electronic or digital pre-press instruction is prepared to the special order of the purchasercustomer.</u> The electronic or d <u>Digital pre-press instruction shall not, however, be regarded as a custom computer program if it is a "canned" or prewritten computer program which is held or existing for general or repeated sale or lease, even if the electronic or digital pre-press instruction was initially developed on a custom basis or for in-house use. The sale of such canned or prewritten digital pre-press instruction in tangible form is a sale of tangible personal property, the retail sale of which is subject to tax.</u></p> <p><u>(g)(h) MAILING.</u> Tax does not apply to charges for postage or for addressing for the purpose of mailing (by hand or by mechanical means), folding for the purpose of mailing, enclosing, sealing, preparing for mailing, or mailing letters or other printed matters, provided such charges are stated separately on invoices and in the accounting records. Tax applies, however, to charges for envelopes.</p> <p><u>(h)(i) SIGNS, SHOW CARDS, AND POSTERS.</u> Tax applies to retail sales of signs, show cards, and posters, and to charges for painting signs, show cards, and posters, whether the materials are furnished by the painter or by the customer.</p> <p>Tax does not apply to charges for painting or lettering on real property. The painter or letterer is the consumer of the materials used in such work, and tax applies with respect to the sale of such property to <u>or the use of such property by, the painter or letterer him.</u></p>

AGENDA C— February 5, 2002 Business Taxes Committee Meeting
Graphic Arts and Related Enterprises - Regulation 1541, Printing and Related Arts

Action Item	Current Regulatory Language	Regulatory Language Proposed by Staff	Regulatory Language Proposed by Patrick Leone (Alternative 6)
Action 2 - Special Printing Aids	<p>Regulation 1541. PRINTING AND RELATED ARTS.</p> <p><u>(c) SPECIAL PRINTING AIDS. In General. In recognition of the unique utility that special printing aids have to the sale of printed material, and the need to avoid burdening businesses with unnecessary paperwork, the following presumptions shall apply.</u></p> <p>(1) With respect to sales of printed material ultimately subject to sales tax, or sales to the U. S. Government, it shall be presumed that the selling price of the printed material includes the selling price of the special printing aids and that title passed to the customer, irrespective of whether or not the printer separately itemizes the special printing aids. It shall be further presumed that the printer, or other reseller, discussed in the following paragraph, made no use of the special printing aids prior to their sale. Accordingly the printer may purchase the special printing aids for resale.</p> <p>“Ultimately subject to sales tax,” means either the printer's sale of the printed material and special printing aids is subject to sales tax or is an exempt sale to the U. S. Government, or if the printer's sale of the</p>	<p>Regulation 1541. PRINTING AND RELATED ARTS.</p> <p>(c) SPECIAL PRINTING AIDS. In General. In recognition of the unique utility that special printing aids have to the sale of printed material, and the need to avoid burdening businesses with unnecessary paperwork, the following presumptions shall apply.</p> <p>–(1) With respect to sales of printed material ultimately subject to sales tax, or sales to the U. S. Government, it shall be presumed that the selling price of the printed material includes the selling price of the special printing aids and that title passed to the customer, irrespective of whether or not the printer separately itemizes the special printing aids. It shall be further presumed that the printer, or other reseller, discussed in the following paragraph, made no use of the special printing aids prior to their sale. Accordingly the printer may purchase the special printing aids for resale.</p> <p>“Ultimately subject to sales tax,” means either the printer's sale of the printed material and special printing aids is subject to sales tax or is an exempt sale to the U. S. Government, or if the printer's sale of the</p>	<p>Regulation 1541. PRINTING AND RELATED ARTS.</p> <p><u>(c) SPECIAL PRINTING AIDS. In General. In recognition of the unique utility that special printing aids have to the sale of printed material, and the need to avoid burdening businesses with unnecessary paperwork, the following presumptions shall apply.</u></p> <p>(1) With respect to sales of printed material ultimately subject to sales tax, or sales to the U. S. Government, it shall be presumed that the selling price of the printed material includes the selling price of the special printing aids and that title passed to the customer, irrespective of whether or not the printer separately itemizes the special printing aids. It shall be further presumed that the printer, or other reseller, discussed in the following paragraph, made no use of the special printing aids prior to their sale. Accordingly the printer may purchase the special printing aids for resale.</p> <p>“Ultimately subject to sales tax,” means either the printer's sale of the printed material and special printing aids is subject to sales tax or is an exempt sale to the U. S. Government, or if the printer's sale of the</p>

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Action Item	Current Regulatory Language	Regulatory Language Proposed by Staff	Regulatory Language Proposed by Patrick Leone (Alternative 6)
	<p>printed material is for resale, a subsequent sale of the printed material and special printing aids is subject to California sales tax or is an exempt sale to the U. S. Government.</p> <p><u>When the printer's sale of printed material is a sale for resale, as described in the above paragraph, unless the printer timely takes a valid resale certificate in good faith that states the special printing aids are to be purchased for resale, tax is due on the selling price of the special printing aids whether or not the selling price is separately itemized. The selling price of the special printing aids is deemed to be the sales price of the special printing aids, or their components, to the printer regardless of the amount of the separately stated charge, if any, for the special printing aid. The printer need not separately charge sales tax reimbursement to their customer and if the printer has paid sales or use tax on the selling price of the special printing aids or their components to the printer, no additional tax is due.</u></p> <p><u>The term "special printing aids" on a resale certificate shall be sufficient to cover all special printing aids as defined in subdivision (a)(1).</u></p> <p>(2) If a printer does not wish to sell special printing aids in connection with the sale of printed material ultimately subject to sales tax or sold to the U. S.</p>	<p>printed material is for resale, a subsequent sale of the printed material and special printing aids is subject to California sales tax or is an exempt sale to the U. S. Government.</p> <p><u>When the printer's sale of printed material is a sale for resale, as described in the above paragraph, unless the printer timely takes a valid resale certificate in good faith that states the special printing aids are to be purchased for resale, tax is due on the selling price of the special printing aids whether or not the selling price is separately itemized. The selling price of the special printing aids is deemed to be the sales price of the special printing aids, or their components, to the printer regardless of the amount of the separately stated charge, if any, for the special printing aid. The printer need not separately charge sales tax reimbursement to their customer and if the printer has paid sales or use tax on the selling price of the special printing aids or their components to the printer, no additional tax is due.</u></p> <p><u>The term "special printing aids" on a resale certificate shall be sufficient to cover all special printing aids as defined in subdivision (a)(1).</u></p> <p>—(2) If a printer does not wish to sell special printing aids in connection with the sale of printed material ultimately subject to sales tax or sold to the U. S.</p>	<p>printed material is for resale, a subsequent sale of the printed material and special printing aids is subject to California sales tax or is an exempt sale to the U. S. Government.</p> <p><u>When the printer's sale of printed material is a sale for resale, as described in the above paragraph, unless the printer timely takes a valid resale certificate in good faith that states the special printing aids are to be purchased for resale, tax is due on the selling price of the special printing aids whether or not the selling price is separately itemized. The selling price of the special printing aids is deemed to be the sales price of the special printing aids, or their components, to the printer regardless of the amount of the separately stated charge, if any, for the special printing aid. The printer need not separately charge sales tax reimbursement to their customer and if the printer has paid sales or use tax on the selling price of the special printing aids or their components to the printer, no additional tax is due.</u></p> <p><u>The term "special printing aids" on a resale certificate shall be sufficient to cover all special printing aids as defined in subdivision (a)(1).</u></p> <p>(2) If a printer does not wish to sell special printing aids in connection with the sale of printed material ultimately subject to sales tax or sold to the U. S.</p>

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Action Item	Current Regulatory Language	Regulatory Language Proposed by Staff	Regulatory Language Proposed by Patrick Leone (Alternative 6)
	<p>Government, described in (c)(1) above, the following statement should be included on the sales invoice: “The selling price of the printed material does not include the transfer of title to the special printing aids.” The printer would then be the owner and consumer of the special printing aids. Tax would apply to both the retail sale of the printed material and the cost to the printer of the special printing aids.</p> <p><u>(3) With respect to all other sales of printed material, as for example, sales in interstate commerce, sales of exempt newspapers or periodicals, or sales of exempt printed sales messages, it shall also be presumed that the selling price of the printed material includes the selling price of the special printing aids and that title passed to the customer irrespective of whether or not the printer separately itemizes the special printing aids. It shall be further presumed that the printer made no use of the special printing aids prior to their sale. Sales tax is due on the selling price of the special printing aids whether or not the selling price of the special printing aids is separately stated. The selling price of the special printing aids is deemed to be the sales price of the special printing aids, or their components, to the printer regardless of the amount of the separately stated charge, if any, for the special printing aid.</u></p> <p>The printer need not separately charge sales tax reimbursement to their customer and if</p>	<p>Government, described in (c)(1) above, the following statement should be included on the sales invoice: “The selling price of the printed material does not include the transfer of title to the special printing aids.” The printer would then be the owner and consumer of the special printing aids. Tax would apply to both the retail sale of the printed material and the cost to the printer of the special printing aids.</p> <p><u>(3) With respect to all other sales of printed material, as for example, sales in interstate commerce, sales of exempt newspapers or periodicals, or sales of exempt printed sales messages, it shall also be presumed that the selling price of the printed material includes the selling price of the special printing aids and that title passed to the customer irrespective of whether or not the printer separately itemizes the special printing aids. It shall be further presumed that the printer made no use of the special printing aids prior to their sale. Sales tax is due on the selling price of the special printing aids whether or not the selling price of the special printing aids is separately stated. The selling price of the special printing aids is deemed to be the sales price of the special printing aids, or their components, to the printer regardless of the amount of the separately stated charge, if any, for the special printing aid.</u></p> <p>The printer need not separately charge sales tax reimbursement to their customer and if</p>	<p>Government, described in (c)(1) above, the following statement should be included on the sales invoice: “The selling price of the printed material does not include the transfer of title to the special printing aids.” The printer would then be the owner and consumer of the special printing aids. Tax would apply to both the retail sale of the printed material and the cost to the printer of the special printing aids.</p> <p><u>(3) With respect to all other sales of printed material, as for example, sales in interstate commerce, sales of exempt newspapers or periodicals, or sales of exempt printed sales messages, it shall also be presumed that the selling price of the printed material includes the selling price of the special printing aids and that title passed to the customer irrespective of whether or not the printer separately itemizes the special printing aids. It shall be further presumed that the printer made no use of the special printing aids prior to their sale. Sales tax is due on the selling price of the special printing aids whether or not the selling price of the special printing aids is separately stated. The selling price of the special printing aids is deemed to be the sales price of the special printing aids, or their components, to the printer regardless of the amount of the separately stated charge, if any, for the special printing aid.</u></p> <p>The printer need not separately charge sales tax reimbursement to their customer and if</p>

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	<p>the printer has paid sales or use tax on the selling price of the special printing aids or their components to the printer, no additional tax is due.</p> <p><u>However, sales tax is not due on the selling price of the special printing aids discussed in (c)(3) if the printer timely takes a valid resale certificate in good faith that states the special printing aids are to be purchased for resale. The term “special printing aids” on a resale certificate shall be sufficient to cover all special printing aids as defined in subdivision (a)(1).</u></p> <p><u>Persons issuing resale certificates for special printing aids as discussed in (c)(3) are then liable for the tax on their selling price of the special printing aids irrespective of whether or not the printer separately itemized the printing aids to the person issuing the resale certificate and notwithstanding that the printed material is exempt from tax as for example, a sale in interstate commerce, a sale of exempt newspapers or periodicals or a sale of exempt printed sales messages. In no event shall the selling price of the special printing aids be less than the selling price of the special printing aids, or their components, to the printer.</u></p> <p>If the printer’s sale includes both a sale of printed material ultimately subject to sales tax, as described in (c)(1) above, and a sale of printed material as described in (c)(3)</p>	<p>the printer has paid sales or use tax on the selling price of the special printing aids or their components to the printer, no additional tax is due.</p> <p><u>However, sales tax is not due on the selling price of the special printing aids discussed in (c)(3) if the printer timely takes a valid resale certificate in good faith that states the special printing aids are to be purchased for resale. The term “special printing aids” on a resale certificate shall be sufficient to cover all special printing aids as defined in subdivision (a)(1).</u></p> <p><u>Persons issuing resale certificates for special printing aids as discussed in (c)(3) are then liable for the tax on their selling price of the special printing aids irrespective of whether or not the printer separately itemized the printing aids to the person issuing the resale certificate and notwithstanding that the printed material is exempt from tax as for example, a sale in interstate commerce, a sale of exempt newspapers or periodicals or a sale of exempt printed sales messages. In no event shall the selling price of the special printing aids be less than the selling price of the special printing aids, or their components, to the printer.</u></p> <p>If the printer’s sale includes both a sale of printed material ultimately subject to sales tax, as described in (c)(1) above, and a sale of printed material as described in (c)(3)</p>	<p>the printer has paid sales or use tax on the selling price of the special printing aids or their components to the printer, no additional tax is due.</p> <p><u>However, sales tax is not due on the selling price of the special printing aids discussed in (c)(3) if the printer timely takes a valid resale certificate in good faith that states the special printing aids are to be purchased for resale. The term “special printing aids” on a resale certificate shall be sufficient to cover all special printing aids as defined in subdivision (a)(1).</u></p> <p><u>Persons issuing resale certificates for special printing aids as discussed in (c)(3) are then liable for the tax on their selling price of the special printing aids irrespective of whether or not the printer separately itemized the printing aids to the person issuing the resale certificate and notwithstanding that the printed material is exempt from tax as for example, a sale in interstate commerce, a sale of exempt newspapers or periodicals or a sale of exempt printed sales messages. In no event shall the selling price of the special printing aids be less than the selling price of the special printing aids, or their components, to the printer.</u></p> <p>If the printer’s sale includes both a sale of printed material ultimately subject to sales tax, as described in (c)(1) above, and a sale of printed material as described in (c)(3)</p>

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	<p>("split sale"), tax is due on the selling price of the special printing aids. Absent a separate itemization, as long as tax is reported on an amount equal to at least the selling price of the special printing aids or their components to the printer, no further tax will be due on the selling price of the special printing aids.</p> <p><u>(4) If a printer does not wish to sell special printing aids in connection with all other sales of printed material, as discussed in (c)(3) above, the following statement should be included on the sales invoice: "The selling price of the printed material does not include the transfer of title to the special printing aids." The printer would then be the owner and consumer of the special printing aids. Tax would apply to the cost to the printer of the special printing aids.</u></p> <p><u>(5) No other proof shall be required with respect to passage of title on special printing aids.</u></p>	<p>("split sale"), tax is due on the selling price of the special printing aids. Absent a separate itemization, as long as tax is reported on an amount equal to at least the selling price of the special printing aids or their components to the printer, no further tax will be due on the selling price of the special printing aids.</p> <p><u>(4) If a printer does not wish to sell special printing aids in connection with all other sales of printed material, as discussed in (c)(3) above, the following statement should be included on the sales invoice: "The selling price of the printed material does not include the transfer of title to the special printing aids." The printer would then be the owner and consumer of the special printing aids. Tax would apply to the cost to the printer of the special printing aids.</u></p> <p><u>(5) No other proof shall be required with respect to passage of title on special printing aids.</u></p> <p>(c) SPECIAL PRINTING AIDS. In recognition of the unique utility that special printing aids have to the production of printed matter, the practices of the industry, and the need to avoid burdening businesses with unnecessary paperwork, the presumptions and rules set forth in this subdivision apply to a printer's purchase and sale of special printing aids used to produce printed matter sold by the printer.</p>	<p>("split sale"), tax is due on the selling price of the special printing aids. Absent a separate itemization, as long as tax is reported on an amount equal to at least the selling price of the special printing aids or their components to the printer, no further tax will be due on the selling price of the special printing aids.</p> <p><u>(4) If a printer does not wish to sell special printing aids in connection with all other sales of printed material, as discussed in (c)(3) above, the following statement should be included on the sales invoice: "The selling price of the printed material does not include the transfer of title to the special printing aids." The printer would then be the owner and consumer of the special printing aids. Tax would apply to the cost to the printer of the special printing aids.</u></p> <p><u>(5) No other proof shall be required with respect to passage of title on special printing aids.</u></p> <p>(c) SPECIAL PRINTING AIDS. In recognition of the unique utility that special printing aids have to the production of printed matter, the practices of the industry, and the need to avoid burdening businesses with unnecessary paperwork, the presumptions and rules set forth in this subdivision apply to a printer's purchase and sale of special printing aids used to produce printed matter sold by the printer.</p>

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		<p><u>(1) PRINTER'S PURCHASE OF SPECIAL PRINTING AIDS.</u></p> <p><u>(A) When a printer who uses special printing aids to produce printed matter does not wish to sell those special printing aids in connection with the printer's sale of the printed matter so produced, the printer shall include the following or substantially similar statement in the contract or the sales invoice: "Special printing aids are not being sold to the customer as part of the sale of the printed matter, and the selling price of the printed matter does not include the transfer of title to the special printing aids." When this statement, or a substantially similar statement, is included in the contract or sales invoice, the printer retains title to the special printing aids and is the consumer thereof, without regard to whether the printer separately itemizes a charge for the special printing aids. Accordingly, the printer may not issue a resale certificate to purchase such special printing aids for resale, and tax applies to the cost to the printer of those special printing aids.</u></p> <p><u>(B) Unless the printer includes a statement in the contract or sales invoice retaining title to the special printing aids, as described in subdivision (c)(1)(A), it shall be irrebuttably presumed that the printer resold to the customer the special printing aids purchased or produced by the printer</u></p>	<p><u>(1) PRINTER'S PURCHASE OF SPECIAL PRINTING AIDS.</u></p> <p><u>(A) When a printer who uses special printing aids to produce printed matter does not wish to sell those special printing aids in connection with the printer's sale of the printed matter so produced, the printer shall include the following or substantially similar statement in the contract or the sales invoice: "Special printing aids are not being sold to the customer as part of the sale of the printed matter, and the selling price of the printed matter does not include the transfer of title to the special printing aids." When this statement, or a substantially similar statement, is included in the contract or sales invoice, the printer retains title to the special printing aids and is the consumer thereof, without regard to whether the printer separately itemizes a charge for the special printing aids. Accordingly, the printer may not issue a resale certificate to purchase such special printing aids for resale, and tax applies to the cost to the printer of those special printing aids.</u></p> <p><u>(B) Unless the printer includes a statement in the contract or sales invoice retaining title to the special printing aids, as described in subdivision (c)(1)(A), it shall be irrebuttably presumed that the printer resold to the customer the special printing aids purchased or produced by the printer</u></p>

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		<p>for use on the customer's job, prior to any use, along with the printed matter produced with the special printing aids, without regard to whether the printer separately itemizes a charge for the special printing aids. Accordingly, unless the printer includes a statement in the contract or sales invoice retaining title, the printer may issue a resale certificate when purchasing such special printing aids or their components. If the vendor of the special printing aids to the printer does not take a valid and timely resale certificate from the printer stating that the special printing aids are for resale, the vendor has the burden of showing that the printer actually resold the special printing aids prior to use as provided in this subdivision.</p> <p><u>(2) PRINTER'S SALE OF SPECIAL PRINTING AIDS.</u> When the printer is regarded as purchasing the special printing aids for resale under subdivision (c)(1)(B), the following rules apply to determine the application of tax to the printer's sale of those special printing aids along with the printed matter produced with the special printing aids.</p> <p><u>(A) Retail Sales of Special Printing Aids.</u></p> <p>1. Sales to the United States Government. When a printer makes a retail sale of special printing aids along with the printed matter produced with those special</p>	<p>for use on the customer's job, prior to any use, along with the printed matter produced with the special printing aids, without regard to whether the printer separately itemizes a charge for the special printing aids. Accordingly, unless the printer includes a statement in the contract or sales invoice retaining title, the printer may issue a resale certificate when purchasing such special printing aids or their components. If the vendor of the special printing aids to the printer does not take a valid and timely resale certificate from the printer stating that the special printing aids are for resale, the vendor has the burden of showing that the printer actually resold the special printing aids prior to use as provided in this subdivision.</p> <p><u>(2) PRINTER'S SALE OF SPECIAL PRINTING AIDS.</u> When the printer is regarded as purchasing the special printing aids for resale under subdivision (c)(1)(B), the following rules apply to determine the application of tax to the printer's sale of those special printing aids along with the printed matter produced with the special printing aids.</p> <p><u>(A) Retail Sales of Special Printing Aids.</u></p> <p>1. Sales to the United States Government. When a printer makes a retail sale of special printing aids along with the printed matter produced with those special</p>

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		<p>printing aids to the United States Government, the sale of the printed matter and the special printing aids to the United States Government is exempt from tax as provided in Regulation 1614.</p> <p>2. With nontaxable sale of printed matter. When a printer makes a retail sale of special printing aids to anyone other than the United States Government along with a nontaxable sale of printed matter (such as an exempt sale in interstate commerce, an exempt sale of qualifying newspapers, periodicals, or printed sales messages, or a nontaxable sale for resale), the printer's sale of the special printing aids is subject to sales tax. The printer's taxable gross receipts or sales price from the sale of the special printing aids is deemed to be the sale price of the special printing aids, or their components, to the printer without regard to whether the printer separately states a charge for the special printing aids or, if the printer does so, without regard to the amount of that separately stated charge, and tax is due measured by that sale price. If the printer has paid California sales tax reimbursement or use tax on the sale price of the special printing aids or their components to the printer, no additional tax is due.</p> <p>3. With taxable sale of printed matter. When a printer makes a retail sale of special printing aids along with the taxable</p>	<p>printing aids to the United States Government, the sale of the printed matter and the special printing aids to the United States Government is exempt from tax as provided in Regulation 1614.</p> <p>2. With nontaxable sale of printed matter. When a printer makes a retail sale of special printing aids to anyone other than the United States Government along with a nontaxable sale of printed matter (such as an exempt sale in interstate commerce, an exempt sale of qualifying newspapers, periodicals, or printed sales messages, or a nontaxable sale for resale), the printer's sale of the special printing aids is subject to sales tax. The printer's taxable gross receipts or sales price from the sale of the special printing aids is deemed to be the sale price of the special printing aids, or their components, to the printer without regard to whether the printer separately states a charge for the special printing aids or, if the printer does so, without regard to the amount of that separately stated charge, and tax is due measured by that sale price. If the printer has paid California sales tax reimbursement or use tax on the sale price of the special printing aids or their components to the printer, no additional tax is due.</p> <p>3. With taxable sale of printed matter. When a printer makes a retail sale of special printing aids along with the taxable</p>

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		<p>retail sale of printed matter, tax applies to the entire charge for the printed matter and special printing aids, without regard to <u>whether the charge for the special printing aids is separately stated. If the printer does not make a separate charge for the special printing aids, the charge for the printed matter is deemed to include the taxable charge for the special printing aids, and no further tax is due on account of the sale of those special printing aids.</u></p> <p><u>(B) Nontaxable Sales of Special Printing Aids for Resale.</u> A person purchasing printed matter for resale may also purchase the special printing aids used to produce the printed matter for resale if that person will, in fact, resell the special printing aids prior to any use. A printer will not be regarded as selling special printing aids for resale unless: 1) the printer separately states the sale price of the special printing aids in an amount not less than the sale price of the special printing aids, or their components, to the printer; and 2) the printer accepts a timely and valid resale certificate in good faith from the printer's customer stating that the special printing aids are purchased for resale. The term "special printing aids" on a resale certificate shall be sufficient to cover all special printing aids as defined in subdivision (a)(12), and a printer accepting such a resale certificate in good faith will be regarded as selling the special printing aids for resale provided the printer includes</p>	<p>retail sale of printed matter, tax applies to the entire charge for the printed matter and special printing aids, without regard to <u>whether the charge for the special printing aids is separately stated. If the printer does not make a separate charge for the special printing aids, the charge for the printed matter is deemed to include the taxable charge for the special printing aids, and no further tax is due on account of the sale of those special printing aids.</u></p> <p><u>(B) Nontaxable Sales of Special Printing Aids for Resale.</u> A person purchasing printed matter for resale may also purchase the special printing aids used to produce the printed matter for resale if that person will, in fact, resell the special printing aids prior to any use. A printer will not be regarded as selling special printing aids for resale unless: 1) <u>operative October 1, 2002,</u> the printer separately states the sale price of the special printing aids in an amount not less than the sale price of the special printing aids, or their components, to the printer; and 2) the printer accepts a timely and valid resale certificate in good faith from the printer's customer stating that the special printing aids are purchased for resale. The term "special printing aids" on a resale certificate shall be sufficient to cover all special printing aids as defined in subdivision (a)(12), and a printer accepting such a resale certificate in good faith will be regarded as selling the special printing</p>

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Action Item	Current Regulatory Language	Regulatory Language Proposed by Staff	Regulatory Language Proposed by Patrick Leone (Alternative 6)
		<p>the required separately stated price for them. Otherwise, the printer will be regarded as selling the special printing aids at retail, and will owe tax on that retail sale accordingly. A printer might sell special printing aids for resale along with printed matter under circumstances where the sale of the printed matter is for resale and also qualifies for exemption, such as a sale in interstate commerce where the purchaser will then resell the printed matter prior to use. However, since a purchaser of special printing aids from a printer would not be regarded as purchasing them for resale unless reselling them as part of the sale of the printed matter produced with those special printing aids, a printer claiming its sale of special printing aids is for resale should take a resale certificate for its sale of the printed matter as well, even if the sale of that printed matter would also qualify for exemption.</p> <p>1. Sales of printed matter to multiple purchasers. A person is not purchasing special printing aids for resale when title to the special printing aids does not pass to that person's customer prior to any use. If that person's customer does not obtain the right to exercise dominion and control over the special printing aids, the person will not be selling the special printing aids to its customer and cannot purchase the special printing aids for resale. A person does not purchase special printing aids for resale</p>	<p>aids for resale provided the printer includes the required separately stated price for them. Otherwise, the printer will be regarded as selling the special printing aids at retail, and will owe tax on that retail sale accordingly. A printer might sell special printing aids for resale along with printed matter under circumstances where the sale of the printed matter is for resale and also qualifies for exemption, such as a sale in interstate commerce where the purchaser will then resell the printed matter prior to use. However, since a purchaser of special printing aids from a printer would not be regarded as purchasing them for resale unless reselling them as part of the sale of the printed matter produced with those special printing aids, a printer claiming its sale of special printing aids is for resale should take a resale certificate for its sale of the printed matter as well, even if the sale of that printed matter would also qualify for exemption.</p> <p>1. Sales of printed matter to multiple purchasers. Operative October 1, 2002, A a person is not purchasing special printing aids for resale when title to the special printing aids does not pass to that person's customer prior to any use. If that person's customer does not obtain the right to exercise dominion and control over the special printing aids, the person will not be selling the special printing aids to its customer and cannot purchase the special printing aids for resale. A person does not</p>

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		<p><u>when the printed matter produced with those special printing aids is sold to several purchasers. For example, a person purchasing newspapers for individual sale cannot purchase special printing aids for resale because the individual purchasers of the newspaper are not also purchasing the special printing aids. A person purchasing posters for sale to the general public is not purchasing special printing aids for resale to the general public. A person purchasing printed cartons to pack items for individual sale is not purchasing the special printing aids used to produce the cartons for resale to the ultimate purchasers of the contents of the carton. In addition to the fact that the multiple purchasers in each of these cases could not at any time be regarded as purchasing the special printing aids, the retail purchaser of the end product is not known at the time the special printing aids are used, meaning that the special printing aids could not in any event be resold to those purchasers prior to use.</u></p> <p><u>2. Existing obligation to resell special printing aids. A person cannot purchase special printing aids for resale when that person does not have an existing obligation to resell those particular special printing aids since, if the purchaser does not have such an existing obligation to resell the special printing aids, the printer will use them on the purchaser's behalf before they could be resold by the purchaser. An</u></p>	<p><u>purchase special printing aids for resale when the printed matter produced with those special printing aids is sold to several purchasers. For example, a person purchasing newspapers for individual sale cannot purchase special printing aids for resale because the individual purchasers of the newspaper are not also purchasing the special printing aids. A person purchasing posters for sale to the general public is not purchasing special printing aids for resale to the general public. A person purchasing printed cartons to pack items for individual sale is not purchasing the special printing aids used to produce the cartons for resale to the ultimate purchasers of the contents of the carton. In addition to the fact that the multiple purchasers in each of these cases could not at any time be regarded as purchasing the special printing aids, the retail purchaser of the end product is not known at the time the special printing aids are used, meaning that the special printing aids could not in any event be resold to those purchasers prior to use.</u></p> <p><u>2. Existing obligation to resell special printing aids. A person cannot purchase special printing aids for resale when that person does not have an existing obligation to resell those particular special printing aids since, if the purchaser does not have such an existing obligation to resell the special printing aids, the printer will use them on the purchaser's behalf before they could be resold by the purchaser. An</u></p>

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		<p><u>existing obligation may be represented by a purchase order, invoice, or other existing agreement, whether oral or in writing. If the existing obligation is an oral agreement, the person purchasing the special printing aids for resale must have some means to establish that the agreement was in existence no later than the time the special printing aids were used in the printing process.</u></p> <p><u>(C) Split Sales. A printer may use special printing aids to produce printed matter where a portion of the sale is taxable and a portion of the sale is not taxable, such as the sale of printed sales messages some of which are delivered as required for exemption by Regulation 1541.5 and some of which are delivered directly to the purchaser. If a printer makes a sale of printed matter where a portion of the sale is taxable and a portion is not taxable along with a retail sale of the special printing aids used to produce that printed matter, tax is due on the full sale price of the special printing aids. If the printer separately states a charge for the special printing aids in an amount not less than the sale price of the special printing aids or their components to the printer, tax applies to that separate charge. In the absence of such a separate charge, the taxable portion of the sale of printed matter will be regarded as including the sale of the special printing aids provided that the measure of tax on that sale is at least equal to the sale price of the</u></p>	<p><u>existing obligation may be represented by a purchase order, invoice, or other existing agreement, whether oral or in writing. If the existing obligation is an oral agreement, the person purchasing the special printing aids for resale must have some means to establish that the agreement was in existence no later than the time the special printing aids were used in the printing process.</u></p> <p><u>(C) Split Sales. A printer may use special printing aids to produce printed matter where a portion of the sale is taxable and a portion of the sale is not taxable, such as the sale of printed sales messages some of which are delivered as required for exemption by Regulation 1541.5 and some of which are delivered directly to the purchaser. If a printer makes a sale of printed matter where a portion of the sale is taxable and a portion is not taxable along with a retail sale of the special printing aids used to produce that printed matter, tax is due on the full sale price of the special printing aids. If the printer separately states a charge for the special printing aids in an amount not less than the sale price of the special printing aids or their components to the printer, tax applies to that separate charge. In the absence of such a separate charge, the taxable portion of the sale of printed matter will be regarded as including the sale of the special printing aids provided that the measure of tax on that sale is at least equal to the sale price of the</u></p>

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Action Item	Current Regulatory Language	Regulatory Language Proposed by Staff	Regulatory Language Proposed by Patrick Leone (Alternative 6)
		<p><u>special printing aids or their components to the printer. If so, no further tax is due for the printer's sale of the special printing aids. If the measure of tax on the sale of the printed matter is less than the sale price of the special printing aids or their components to the printer, then the printer owes tax on the difference.</u></p> <p><u>(3) PURCHASES AND SALES OF SPECIAL PRINTING AIDS BY PRINT BROKERS.</u></p> <p><u>(A) Print Broker's Purchase of Special Printing Aids for Resale. A person who purchases special printing aids for resale with printed matter but who will not itself use those special printing aids in the printing process is a print broker for that purchase and resale. A print broker who will acquire title to special printing aids from a printer or other print broker will be irrebuttably presumed to have resold the special printing aids to the customer, prior to any use, along with the printed matter produced with the special printing aids provided the print broker has, at the time of acquisition of the special printing aids, an existing obligation with a customer for the sale of printed matter and the print broker does not include a statement in the contract or sales invoice retaining title to the special printing aids, as described in subdivision (c)(1)(A). Accordingly, unless the print broker includes a statement in the contract or sales invoice retaining title, the print</u></p>	<p><u>special printing aids or their components to the printer. If so, no further tax is due for the printer's sale of the special printing aids. If the measure of tax on the sale of the printed matter is less than the sale price of the special printing aids or their components to the printer, then the printer owes tax on the difference.</u></p> <p><u>(3) PURCHASES AND SALES OF SPECIAL PRINTING AIDS BY PRINT BROKERS.</u></p> <p><u>(A) Print Broker's Purchase of Special Printing Aids for Resale. A person who purchases special printing aids for resale with printed matter but who will not itself use those special printing aids in the printing process is a print broker for that purchase and resale. A print broker who will acquire title to special printing aids from a printer or other print broker will be irrebuttably presumed to have resold the special printing aids to the customer, prior to any use, along with the printed matter produced with the special printing aids provided the print broker has, at the time of acquisition of the special printing aids, an existing obligation with a customer for the sale of printed matter and the print broker does not include a statement in the contract or sales invoice retaining title to the special printing aids, as described in subdivision (c)(1)(A). Accordingly, unless the print broker includes a statement in the contract or sales invoice retaining title, the print</u></p>

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		<p>broker may purchase such special printing aids for resale pursuant to its existing obligation and issue a resale certificate for both the special printing aids and the printed matter. However, without regard to the taking of a resale certificate, a printer or print broker is regarded as making a retail sale of the special printing aids, and not a sale for resale, unless the printer or print broker separately states the charge for those special printing aids, which charge cannot be less than the sale price of such printing aids, or their components, to the printer.</p> <p><u>(B) Print Broker Issuing Resale Certificate.</u> A print broker who issues a resale certificate for the purchase of special printing aids is liable for tax on the print broker's sale price of the special printing aids, even if the print broker's sale of the printed material produced with the special printing aids is not subject to tax (such as an exempt sale in interstate commerce, an exempt sale of qualifying newspapers, periodicals, or printed sales messages, or a nontaxable sale for resale), unless the print broker sells the special printing aids to the United States Government or to another print broker who issues a timely and valid resale certificate in good faith as provided in this subdivision (c).</p> <p><u>(C) Print Broker's Retail Sales of Special Printing Aids.</u></p> <p>1. Sales to the United States</p>	<p>broker may purchase such special printing aids for resale pursuant to its existing obligation and issue a resale certificate for both the special printing aids and the printed matter. However, without regard to the taking of a resale certificate, a printer or print broker is regarded as making a retail sale of the special printing aids, and not a sale for resale, unless the printer or print broker separately states the charge for those special printing aids, which charge cannot be less than the sale price of such printing aids, or their components, to the printer.</p> <p><u>(B) Print Broker Issuing Resale Certificate.</u> A print broker who issues a resale certificate for the purchase of special printing aids is liable for tax on the print broker's sale price of the special printing aids, even if the print broker's sale of the printed material produced with the special printing aids is not subject to tax (such as an exempt sale in interstate commerce, an exempt sale of qualifying newspapers, periodicals, or printed sales messages, or a nontaxable sale for resale), unless the print broker sells the special printing aids to the United States Government or to another print broker who issues a timely and valid resale certificate in good faith as provided in this subdivision (c).</p> <p><u>(C) Print Broker's Retail Sales of Special Printing Aids.</u></p> <p>1. Sales to the United States</p>

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Action Item	Current Regulatory Language	Regulatory Language Proposed by Staff	Regulatory Language Proposed by Patrick Leone (Alternative 6)
		<p>Government. When a print broker who purchases special printing aids under a resale certificate sells those special printing aids along with the printed matter produced with those special printing aids to the United States Government, the sale of the special printing aids to the United States Government is exempt from tax as provided in Regulation 1614.</p> <p>2. With nontaxable sale of printed matter. When a print broker who purchases special printing aids under a resale certificate makes a retail sale of special printing aids to anyone other than the United States Government along with a sale of printed matter that is not taxable (such as an exempt sale in interstate commerce, an exempt sale of qualifying newspapers, periodicals, or printed sales messages, or a nontaxable sale for resale), that sale of the special printing aids is subject to tax. If the print broker separately states a charge for the special printing aids that is not less the printer's separately stated sale price for the special printing aids to the print broker, then tax applies to that separately stated sale price. Otherwise, tax applies to the the print broker's sale of the special printing aids measured by the printer's separately stated sale price to the print broker.</p> <p>3. With taxable sale of printed matter. When a print broker who purchases special printing aids under a resale certificate makes a retail sale of those special printing</p>	<p>Government. When a print broker who purchases special printing aids under a resale certificate sells those special printing aids along with the printed matter produced with those special printing aids to the United States Government, the sale of the special printing aids to the United States Government is exempt from tax as provided in Regulation 1614.</p> <p>2. With nontaxable sale of printed matter. When a print broker who purchases special printing aids under a resale certificate makes a retail sale of special printing aids to anyone other than the United States Government along with a sale of printed matter that is not taxable (such as an exempt sale in interstate commerce, an exempt sale of qualifying newspapers, periodicals, or printed sales messages, or a nontaxable sale for resale), that sale of the special printing aids is subject to tax. If the print broker separately states a charge for the special printing aids that is not less the printer's separately stated sale price for the special printing aids to the print broker, then tax applies to that separately stated sale price. Otherwise, tax applies to the the print broker's sale of the special printing aids measured by the printer's separately stated sale price to the print broker.</p> <p>3. With taxable sale of printed matter. When a print broker who purchases special printing aids under a resale certificate makes a retail sale of those special printing</p>

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		<p><u>aids along with the taxable retail sale of printed matter, tax applies to the entire charge for the printed matter and special printing aids, without regard to whether the charge for the special printing aids is separately stated. If the print broker does not make a separate charge for the special printing aids, the charge for the printed matter is deemed to include the taxable charge for the special printing aids, and no further tax is due on account of those special printing aids.</u></p> <p><u>4. Split Sales. A print broker may sell special printing aids to produce printed matter the sale of which is partially exempt and partially subject to tax, such as the sale of printed sales messages some of which are delivered as required for exemption by Regulation 1541.5 and some of which are delivered directly to the purchaser. If a print broker makes a sale of printed matter where a portion of the sale is taxable and a portion is not taxable along with a retail sale of the special printing aids used to produce that printed matter, tax is due on the full sale price of the special printing aids. If the print broker separately states a charge for the special printing aids in an amount not less than the printer's separately stated sale price of the special printing aids to the print broker, tax applies to that separate charge. In the absence of such a separate charge, the taxable portion of the sale of printed matter will be regarded as including the sale of the special</u></p>	<p><u>aids along with the taxable retail sale of printed matter, tax applies to the entire charge for the printed matter and special printing aids, without regard to whether the charge for the special printing aids is separately stated. If the print broker does not make a separate charge for the special printing aids, the charge for the printed matter is deemed to include the taxable charge for the special printing aids, and no further tax is due on account of those special printing aids.</u></p> <p><u>4. Split Sales. A print broker may sell special printing aids to produce printed matter the sale of which is partially exempt and partially subject to tax, such as the sale of printed sales messages some of which are delivered as required for exemption by Regulation 1541.5 and some of which are delivered directly to the purchaser. If a print broker makes a sale of printed matter where a portion of the sale is taxable and a portion is not taxable along with a retail sale of the special printing aids used to produce that printed matter, tax is due on the full sale price of the special printing aids. If the print broker separately states a charge for the special printing aids in an amount not less than the printer's separately stated sale price of the special printing aids to the print broker, tax applies to that separate charge. In the absence of such a separate charge, the taxable portion of the sale of printed matter will be regarded as including the sale of the special</u></p>

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Graphic Arts and Related Enterprises - Regulation 1541, Printing and Related Arts

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		<u>printing aids provided that the measure of tax on that sale is at least equal to the printer's separately stated sale price of the special printing aids to the print broker; if so, no further tax is due for the print broker's sale of the special printing aids, but if the measure of tax on the sale of the printed matter is less than the printer's separately stated sale price of the special printing aids to the print broker, then the print broker owes tax on the difference.</u>	<u>printing aids provided that the measure of tax on that sale is at least equal to the printer's separately stated sale price of the special printing aids to the print broker; if so, no further tax is due for the print broker's sale of the special printing aids, but if the measure of tax on the sale of the printed matter is less than the printer's separately stated sale price of the special printing aids to the print broker, then the print broker owes tax on the difference.</u>

1540-1543 IP AGENDA C (1541) for PDF.doc rev. 4-5-01

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AGENDA D — February 5, 2002 Business Taxes Committee Meeting
Graphic Arts and Related Enterprises - Regulation 1540, Advertising Agencies,
Commercial Artists and Designers

<p>Action 1 — Consent Items</p> <p>Agenda D, Pages 8-11</p>	<p>Adopt proposed amendments to Regulation 1540 as agreed upon by industry and staff in regard to content. (For regulation organization differences, see Action 2.)</p>																
<p>Action 2 — Organization of Regulation</p> <p>Subdivisions (b) and (c)</p> <p>Agenda D, Pages 21-48</p>	<p>Adopt either:</p> <ol style="list-style-type: none"> 1) Staff's recommended organization of the regulation, in which subdivision (b), <i>Application of Tax to Activities of Advertising Agencies and Commercial Artists</i>, is followed by subdivision (c), <i>Situations Specific to Advertising Agencies</i>, OR 2) The AAAA's recommended organization, which reverses this sequence. That is, the AAAA places <i>Situations Specific to Advertising Agencies</i> in subdivision (b), and <i>Application of Tax to Activities of Advertising Agencies and Commercial Artists</i> in subdivision (c) (Alternative 5). 																
<p>Action 3 — New Clarifying Language Proposed by Staff</p> <p>Agenda D, Pages:</p> <p>16</p> <p>20</p> <p>25</p> <p>27-28</p> <p>36</p> <p>43-44</p> <p>48</p>	<p>Adopt either:</p> <ol style="list-style-type: none"> 1) The following clarifying language proposed by staff: <table border="0"> <thead> <tr> <th><u>Subdivision</u></th> <th><u>Purpose</u></th> </tr> </thead> <tbody> <tr> <td>(a)(5) -</td> <td>Incorporates "digital pre-press definition.</td> </tr> <tr> <td>(a)(13) -</td> <td>Incorporates definition of "third party."</td> </tr> <tr> <td>(b)(1)(B) -</td> <td>Clarifies application of tax to "digital prepress."</td> </tr> <tr> <td>(b)(1)(G) -</td> <td>Example to clarify application of tax to sales.</td> </tr> <tr> <td>(b)(2)(D)2.b -</td> <td>Clarifies factors used to calculate value of labor.</td> </tr> <tr> <td>(c)(2) -</td> <td>Clarifies application of tax to property used by retailer.</td> </tr> <tr> <td>(e)(3) -</td> <td>Incorporates reference to printed sales messages.</td> </tr> </tbody> </table> <p>OR</p> 2) No clarifying language for the subdivisions referenced above. 	<u>Subdivision</u>	<u>Purpose</u>	(a)(5) -	Incorporates "digital pre-press definition.	(a)(13) -	Incorporates definition of "third party."	(b)(1)(B) -	Clarifies application of tax to "digital prepress."	(b)(1)(G) -	Example to clarify application of tax to sales.	(b)(2)(D)2.b -	Clarifies factors used to calculate value of labor.	(c)(2) -	Clarifies application of tax to property used by retailer.	(e)(3) -	Incorporates reference to printed sales messages.
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AGENDA D— February 5, 2002 Business Taxes Committee Meeting
Graphic Arts and Related Enterprises - Regulation 1540, Advertising Agencies,
Commercial Artists and Designers

<p>Action 4 — Definition of Contract of Sale</p> <p>Subdivision (a)(4)</p> <p>Agenda D, Pages 15-16</p>	<p>Adopt either:</p> <ol style="list-style-type: none"> 1) Staff's recommendation to include a definition of "contract of sale," OR 2) AAAA's recommendation that the definition not be included (Alternative 5).
<p>Action 5 — Definition of Finished Art</p> <p>Subdivision (a)(7)</p> <p>Agenda D, Page 18</p>	<p>Adopt either:</p> <ol style="list-style-type: none"> 1) Staff's recommended definition of finished art, OR 2) Mr. Wayne's recommended definition of finished art that includes "such as preparation of special printing aids" (Alternative 3).
<p>Action 6 — Definition of Intermediate Production Aids</p> <p>Subdivision (a)(9)</p> <p>Agenda D, Page 19</p>	<p>Adopt either:</p> <ol style="list-style-type: none"> 1) Staff's recommended definition of intermediate production aids (used to produce special printing aids), OR 2) Mr. Wayne's recommended definition of intermediate production aids (used to produce finished art) (Alternative 3), OR 3) AAAA's recommended definition of intermediate production aids that includes clip-art (Alternative 5).
<p>Action 7 — Definition of Preliminary Art</p> <p>Subdivision (a)(11)</p> <p>Agenda D, Pages 19-20</p>	<p>Adopt either:</p> <ol style="list-style-type: none"> 1) Staff's recommended definition of preliminary art, OR 2) Mr. Wayne's recommendation that the definition should include the implication that the finished art be prepared by the same business entity preparing the preliminary art (Alternative 3), OR 3) AAAA's recommendation that preliminary art is incidental to the services provided by an advertising agency or commercial artist and not subject to tax (Alternative 5).

AGENDA D— February 5, 2002 Business Taxes Committee Meeting
Graphic Arts and Related Enterprises - Regulation 1540, Advertising Agencies,
Commercial Artists and Designers

<p>Action 8 —Application of Tax to Services – Passage of Title</p> <p>Subdivision (b)(1)(A)1. & 2.</p> <p>Agenda D, Pages 21-24</p>	<p>Adopt either:</p> <ol style="list-style-type: none"> 1) Staff’s recommendation that tax apply to services associated with the creation of artwork when the master agreement or other contract passes title or permanent possession of the tangible artwork to the client, <p>OR</p> <ol style="list-style-type: none"> 2) Mr. Wayne’s recommendation to incorporate language that when preliminary art is not approved the job is called a “killed job” and any resulting charges are nontaxable [(b)(1)(A)1] and a provision that title can pass by means of a title clause in the contract of sale passing title to the client prior to use [(b)(1)(A)2] (Alternative 3), <p>OR</p> <ol style="list-style-type: none"> 3) AAAA’s recommendation to adopt staff’s language with the added provision that preliminary art is incidental to the services provided and not subject to tax. (Alternative 5)
<p>Action 9 —Specific Nontaxable Charges</p> <p>Subdivision (b)(1)(F)</p> <p>Agenda D, Page 26</p>	<p>Adopt either:</p> <ol style="list-style-type: none"> 1) Staff’s recommended definition of nontaxable charges billed by advertising agencies and commercial artists, <p>OR</p> <ol style="list-style-type: none"> 2) Mr. Wayne’s recommendation that, in addition to staff’s list, charges for agent fees be included; and that the nontaxable charges be considered as markup for purposes of calculating the selling price of tangible personal property as provided in subdivision (b)(3) (Alternative 3).
<p>Action 10 —Use of Aids in Creation of Finished Art – Title Clause Agreement</p> <p>Subdivision (b)(2)(A)</p> <p>Agenda D, Page 29</p>	<p>Adopt either:</p> <ol style="list-style-type: none"> 1) Staff’s recommended language, <p>OR</p> <ol style="list-style-type: none"> 2) AAAA’s recommendation, which adopts staff’s language plus a provision that intermediate production aids, title to which are passed to the client, are to be taxed only once (Alternative 5).

AGENDA D— February 5, 2002 Business Taxes Committee Meeting
Graphic Arts and Related Enterprises - Regulation 1540, Advertising Agencies,
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<p>Action 11 —Transfer of Finished Art in Tangible Form – Cost of Special Printing Aids</p> <p>Subdivision (b)(2)(C)</p> <p>Agenda D, Page 34</p>	<p>Adopt either:</p> <ol style="list-style-type: none"> 1) Staff’s recommendation that the taxable measure of finished art billed in lump sum is not less than the cost of the retail sale of finished art, plus the cost of any intermediate production aids and special printing aids, title to which is passed to the client prior to use, <p>OR</p> <ol style="list-style-type: none"> 2) AAAA’s recommendation that this provision be deleted (Alternative 5).
<p>Action 12 —Transfer of Finished Art in Tangible Form – Option to Separately State Special Printing Aids</p> <p>Subdivision (b)(2)(C)</p> <p>Agenda D, Page 34</p>	<p>Adopt either:</p> <ol style="list-style-type: none"> 1) Staff’s recommended language, <p>OR</p> <ol style="list-style-type: none"> 2) Mr. Wayne’s recommendation to adopt staff’s language plus a provision for the option that separately stated intermediate production or special printing aids can be treated as a retail sale or agent transaction (Alternative 3).
<p>Action 13 —Technology Transfer Agreement - Requirement That It Be in Writing</p> <p>Subdivision (b)(2)(D)2.</p> <p>Agenda D, Page 34</p>	<p>Adopt either:</p> <ol style="list-style-type: none"> 1) Staff’s recommendation that technology transfer agreements must be in writing, <p>OR</p> <ol style="list-style-type: none"> 2) Mr. Liao’s recommendation that “any agreement” may qualify as a technology transfer agreement (Alternative 4).
<p>Action 14 —Technology Transfer Agreement – Finished Art Transferred on Computer Storage Media</p> <p>Subdivision (b)(2)(D)2.</p> <p>Agenda D, Page 35</p>	<p>Adopt either:</p> <ol style="list-style-type: none"> 1) Staff’s recommendation that tangible personal property transferred as part of technology transfer agreements be valued in accordance with RTC sections 6011 and 6012, <p>OR</p> <ol style="list-style-type: none"> 2) The Guild’s recommendation that temporary transfers on computer storage media be treated as incidental transfers that are nontaxable (Alternative 1).

AGENDA D— February 5, 2002 Business Taxes Committee Meeting
Graphic Arts and Related Enterprises - Regulation 1540, Advertising Agencies,
Commercial Artists and Designers

<p>Action 15 — Technology Transfer Agreement – Separately Stated Price</p> <p>Subdivision (b)(2)(D)2.a.</p> <p>Agenda D, Page 36</p>	<p>Adopt either:</p> <ol style="list-style-type: none"> 1) Staff’s recommended language, OR 2) Mr. Blonder’s recommendation to clarify that a separately stated fair rental value of temporary possession of finished art is included in the “sales price” (Alternative 2).
<p>Action 16 — Technology Transfer Agreement - Value of Artist’s Labor</p> <p>Subdivision (b)(2)(D)2.c.</p> <p>Agenda D, Pages 37-38</p>	<p>Adopt either:</p> <ol style="list-style-type: none"> 1) Staff’s recommendation that the value of an individual artist’s labor is included in the total “cost of labor,” OR 2) Guild’s recommendation that the value of an individual artist’s labor is excluded from the total “cost of labor” (Alternative 1), OR 3) Mr. Blonder’s recommendation that the value of an individual artist’s labor is excluded from the total “cost of labor” (Alternative 2), OR 4) If staff’s recommendation is adopted, Guild recommends a presumption that the fair market value for such labor is presumed to be \$100 in the absence of evidence of a price charged by that commercial artist (Alternative 1).
<p>Action 17 —Cost of Materials – Includes Those Used as Well as Incorporated</p> <p>Subdivision (b)(2)(D)2.c.</p> <p>Agenda D, Page 37</p>	<p>Adopt either:</p> <ol style="list-style-type: none"> 1) Staff’s recommendation that the “cost of materials” include those that are used or incorporated into the finished art, OR 2) Mr. Liao’s recommendation that the “cost of materials” include only those that are physically incorporated into the finished art (Alternative 4).

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<p>Action 18 —Explanation of Calculation of Sales Price of Other Tangible Personal Property</p> <p>Subdivision (b)(3)</p> <p>Agenda D, Pages 38-39</p>	<p>Adopt either:</p> <ol style="list-style-type: none"> 1) Staff's recommendation to provide clarifying language on the application of tax to sales of other tangible personal property, <p>OR</p> <ol style="list-style-type: none"> 2) AAAA's recommendation to delete this subdivision (Alternative 5).
<p>Action 19 —Evidence to Prove Erroneous Issuance of Resale Certificate</p> <p>Subdivision (c)(1)(C)</p> <p>Agenda D, Pages 42-43</p>	<p>Adopt either:</p> <ol style="list-style-type: none"> 1) Staff's recommendation to explain that an advertising agency that purchases tangible personal property with a resale certificate cannot overcome the presumption that it purchased such property for its own account if it treats the transaction as its own sale of tangible personal property to its client, collecting tax or tax reimbursement on its own behalf from its client on that sale, <p>OR</p> <ol style="list-style-type: none"> 2) AAAA's recommendation to delete the language that provides that if the advertising agency treats the transaction as its own sale of tangible personal property to its client, collecting tax or tax reimbursement from its client on its own behalf, the advertising agency did not act as an agent of its client (Alternative 5).
<p>Action 20 —Invoice to Client for More Than Cost of Property</p> <p>Subdivision (c)(2)(C)</p> <p>Agenda D, Pages 47-48</p>	<p>Adopt either:</p> <ol style="list-style-type: none"> 1) Staff's recommendation to provide clarifying language on the application of tax to sales of tangible personal property when the invoice to the client is more than the cost of the tangible personal property to the advertising agency, <p>OR</p> <ol style="list-style-type: none"> 2) AAAA's recommendation to delete the language on the application of tax to sales of tangible personal property when the invoice to the client is more than the cost of the tangible personal property to the advertising agency (Alternative 5).

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<p>Action 21 — General Language Differences</p> <p>Subdivisions:</p> <p>(a)(1), (a)(2), (a)(3), (a)(6), (a)(7); (b)(1)(A)1., (b)(1)(B), (b)(1)(F), (b)(1)(F)1. & 2., (b)(2)(B), (b)(2)(C), (b)(2)(D)2.a., (b)(2)(D)2.c., (b)(4); (c)(1), (c)(1)(A), (c)(2)(A), (c)(2)(B); (e)(5)</p> <p>Agenda D, Pages:</p> <p>12, 13, 17, 18; 21, 25, 26-27, 29 & 31, 32, 36, 38, 40; 41, 45, 46; 49</p>	<p>Adopt either:</p> <p>1) Staff's recommended language in subdivisions noted at left, OR 2) Guild's recommended language in subdivision (b)(2)(D)2.a. (Alternative 1), OR 3) Mr. Wayne's recommended language in subdivision (c)(2)(B) (Alternative 3), OR 4) AAAA's recommended language in all subdivisions noted at left except (b)(2)(D)2.a. (Alternative 5).</p>
<p>Action 22 — Authorization to Publish</p> <p>(whichever language is approved)</p>	<p>Recommend the publication of the proposed amendments to Regulation 1540 as adopted in the above actions.</p> <p>Operative Date: None Implementation: 30 days following OAL approval</p>

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Action Item	Staff and Industry's Proposed Regulatory Language
<p>Action 1 — Consent Items</p> <p>In Regard to Content (For regulation organization differences, see Action 2.)</p>	<p>Regulation 1540. ADVERTISING AGENCIES <u>AND</u>, COMMERCIAL ARTISTS AND DESIGNERS.</p> <p>(a) DEFINITIONS.</p> <p><i>(a)(1) through (a)(7) are nonconsent items</i></p> <p>(8) HARD COPIES. An item is transferred on hard copy when it is transferred on any tangible personal property other than in digital format on electronic media. For example, finished art transferred on canvas or paper is transferred on hard copy while a transfer of finished art in digital format on compact or floppy disc is not regarded as a transfer on hard copy.</p> <p><i>(a)(9) is a nonconsent item</i></p> <p>(10) MASTER AGREEMENT. A master agreement is a contract, however characterized (such as “agency-client agreement”), entered into between an advertising agency or commercial artist and its client which specifies the obligations of each party to the master agreement with respect to their relationship, whether for a specified time or advertising campaign or until one of the parties terminates the agreement. After entering into a master agreement, the parties may thereafter enter into additional contracts, including fulfillment of purchase orders issued by the client for the purchase of specific services, tangible personal property, or both, which additional contracts include all the terms in the master agreement which are not explicitly in conflict with the later contracts.</p> <p><i>(a)(11) is a nonconsent item</i></p> <p>(12) SPECIAL PRINTING AIDS. Special printing aids are reusable manufacturing aids which are used by a printer during the printing process and are of unique utility to a particular client. Special printing aids include electrotypes, stereotypes, photoengravings, silk screens, steel dies, cutting dies, lithographic plates, film, single or multi color separation negatives, and flats.</p> <p><i>(a)(13) is a nonconsent item</i></p> <p>(b) APPLICATION OF TAX TO ACTIVITIES OF ADVERTISING AGENCIES AND COMMERCIAL ARTISTS.</p> <p>(1) SERVICES.</p> <p><i>(b)(1)(A) through (b)(1)(B) are nonconsent items</i></p>

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Action Item	Staff and Industry's Proposed Regulatory Language
	<p>(C) Retouching Photographic Images. Retouching a photographic image for the purpose of repairing or restoring the photograph to its original condition is a repair, the charge for which is not taxable.</p> <p>(D) Signage. The creation and providing of single copies of blueprints, diagrams, and instructions for signage as a result of environmental graphic design is a service the charge for which is not taxable. Charges for additional copies are taxable.</p> <p>(E) Websites. The design, editing, or hosting of an electronic website in which no tangible personal property is transferred to the client is a service, the charge for which is not subject to tax.</p> <p><i>(b)(1)(F), (F)1. and (F)2. are nonconsent items</i></p> <p>(F) Specific Nontaxable Charges.</p> <p>3. Consultation and concept development fees related to client discussion, development of ideas, and other services. If the advertising agency transfers to the client tangible personal property produced as a result of these services, the transfer is incidental to the advertising agency's providing of the service and is not a sale of that tangible personal property; the advertising agency is the consumer of tangible personal property transferred to the client incidental to the providing of a service.</p> <p>4. Fees for research or account planning that entail consumer research and the application of that research to the client's business or industry.</p> <p>5. Fees for quality control supervision that entails the proofing and review of printing and other products provided by outside suppliers.</p> <p>6. Charges for the formulation and writing of copy.</p> <p><i>(b)(1)(G) is a nonconsent item</i></p> <p>(b)(2) FINISHED ART.</p> <p>(A) Use of Aids in Creation of Finished Art. If the advertising agency or commercial artist uses any intermediate production aids or special printing aids in the creation of the finished art, the presumptions with respect to passage of title and the calculation of the measure of tax on the sale of such aids by the advertising agency or commercial artist, is</p>

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	<p>governed by the provisions of Regulation 1541 applicable to special printing aids.</p> <p><i>(b)(2)(A)1., (b)(2)(B) and (C) are nonconsent items</i></p> <p>(D) Reproduction Rights Transferred With Finished Art.</p> <p>1. Charges for the transfer of possession in tangible form to the client or to anyone else on the client's behalf of finished art for purposes of reproduction are included in the measure of tax on that sale, including all charges for the right to use that property, even though there is no transfer of title to the person reproducing the finished art, except as provided in subdivision (b)(2)(D)2.</p> <p><i>(b)(2)(D)2. is nonconsent</i></p> <p><i>(b)(3) and (b)(4) are nonconsent items</i></p> <p>(c) SITUATIONS SPECIFIC TO ADVERTISING AGENCIES.</p> <p>(1) ADVERTISING AGENCY ACTING AS AN AGENT FOR ITS CLIENT</p> <p><i>(c)(1) and (c)(1)(A) are nonconsent items</i></p> <p>(B) When an advertising agency is the agent of its client for the purchase of tangible personal property under subdivision (c)(1), sales or use tax is due on the purchase price from the supplier to the advertising agency. Tax does not apply to the charge made by an advertising agency to its client for reimbursement, including tax reimbursement, for the amount charged by a supplier, nor does tax apply to the advertising agency's separately stated charges for its services directly related to its acquisition of such tangible personal property (e.g., when the advertising agency makes a separately itemized charge for reimbursement of the amount paid to the supplier of the property, tax does not apply to a separately itemized "agency fee"). When the applicable tax is use tax and the advertising agency does not pay that use tax to the supplier on the client's behalf, the advertising agency is liable for the use tax and must report and pay the use tax to the Board. The advertising agency's liability for that use tax is not extinguished unless the client has self-reported and paid the tax to the Board.</p> <p><i>(c)(1)(C) is a nonconsent item</i></p> <p><i>(c)(2) through (c)(2)(C) are nonconsent items</i></p>

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Action Item	Staff and Industry's Proposed Regulatory Language
	<p>(d) TRANSFERS BY AN ARTIST AT A SOCIAL GATHERING. The transfer of original drawings, sketches, illustrations, or paintings by an artist at a social gathering for entertainment purposes is not a sale or use or purchase of tangible personal property, and the artist is the consumer of any property so transferred, when all the following requirements are satisfied:</p> <p>(1) Eighty percent or more of the drawings, sketches, illustrations, or paintings are delivered by the artist to a person or persons other than the purchaser;</p> <p>(2) Eighty percent or more of all of the drawings, sketches, illustrations, or paintings are received by a person or persons, other than the purchaser, at no cost to the person or persons who become the owner of the drawings, sketches, illustrations, or paintings;</p> <p>(3) The charge for the drawings, sketches, illustrations, or paintings is based on a preset fee; and</p> <p>(4) The preset fee charged for the drawings, sketches, illustrations, or paintings is contingent upon a minimum number of at least three drawings, sketches, illustrations, or paintings to be produced by the artist at the social gathering.</p> <p>(e) CHARGES AND TRANSACTIONS GOVERNED BY OTHER REGULATIONS.</p> <p>(1) AUDIO PRODUCTIONS. Tax applies to charges for an audio production obtained or furnished by an advertising agency to its client as provided in Regulation 1527.</p> <p>(2) PHOTOGRAPHY. Tax applies to charges for photography as provided in Regulation 1528 except when the photographic image is furnished by a commercial artist as defined in subdivision (a)(3).</p> <p><i>(e)(3) is a nonconsent item</i></p> <p>(4) TYPOGRAPHY. Tax applies to charges for typography or composed type obtained from outside suppliers as provided in Regulation 1541.</p> <p><i>(e)(5) is a nonconsent item</i></p>

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2Action Item *	Regulatory Language Proposed by Staff	Regulatory Language Proposed by Guild (Alternative 1)	Regulatory Language Proposed by Blonder (Alternative 2)	Regulatory Language Proposed by Wayne (Alternative 3)	Regulatory Language Proposed by Liao (Alternative 4)	Regulatory Language Proposed by AAAA (Alternative 5)
ACTION 2 - Organization of Regulation	<i>Note – Staff provided revised language to interested parties on 12-19-01.</i>	<i>Note – Alternative language is on pages 34-38.</i>	<i>Note – Alternative language is on pages 36-37.</i>	<i>Note – Alternative language begins on page 18 and continues throughout table.</i>	<i>Note – Mr. Liao did not respond to staff's revised language. Alternative language is on pages 34-38.</i>	<i>AAAA proposes an organization for Regulation 1540 that is different from staff's and other alternatives. The primary difference is the reversal of major sections (b) and (c).</i>
ACTION 21 - General Language Differences	Regulation 1540. ADVERTISING AGENCIES AND COMMERCIAL ARTISTS AND DESIGNERS. (a) DEFINITIONS. (1) ADVERTISING. Advertising is commercial communication utilizing one or more forms of communication (such as television, print, billboards, or the Internet) from or on behalf of an identified person to an intended target audience. (2) ADVERTISING AGENCIES. Advertising agencies design and	Regulation 1540. ADVERTISING AGENCIES AND COMMERCIAL ARTISTS AND DESIGNERS. (a) DEFINITIONS. [same as staff's] [same as staff's]	Regulation 1540. ADVERTISING AGENCIES AND COMMERCIAL ARTISTS AND DESIGNERS. (a) DEFINITIONS. [same as staff's] [same as staff's]	Regulation 1540. ADVERTISING AGENCIES AND COMMERCIAL ARTISTS AND DESIGNERS. (a) DEFINITIONS. [same as staff's] [same as staff's]	Regulation 1540. ADVERTISING AGENCIES AND COMMERCIAL ARTISTS AND DESIGNERS. (a) DEFINITIONS. [no comments received] [no comments received]	Regulation 1540. ADVERTISING AGENCIES AND COMMERCIAL ARTISTS AND DESIGNERS. (a) DEFINITIONS. (1) ADVERTISING. Advertising is commercial communication utilizing one or more forms of communication (such as television, print, billboards, or the Internet) from or on behalf of an identified person or entity to an intended target audience. (2) ADVERTISING AGENCIES. Advertising agencies design and

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2Action Item *	Regulatory Language Proposed by Staff	Regulatory Language Proposed by Guild (Alternative 1)	Regulatory Language Proposed by Blonder (Alternative 2)	Regulatory Language Proposed by Wayne (Alternative 3)	Regulatory Language Proposed by Liao (Alternative 4)	Regulatory Language Proposed by AAAA (Alternative 5)
ACTION 21 - General Language Differences	implement advertising campaigns for purposes of advertising the goods, services, or ideas of their clients. As part of that primary function, advertising agencies provide their clients with services (such as consultation, consumer research, media planning and placement, public relations, and other marketing activities) and tangible personal property (such as print advertisements, finished art, and video and audio productions).					implement advertising campaigns for purposes of advertising the goods, services, or ideas of their clients. As part of that primary function, advertising agencies provide their clients with services (such as consultation, consumer research, and media planning, television and radio commercials, print advertising, brand advertising, website design, internet design, public relations and development of marketing, communication programs) —and tangible personal property (such as print advertisements, finished art, and video and audio productions). Incidental to these services, the advertising agencies may provide some tangible personal property to the client.
ACTION 21 - General Language Differences	(3) COMMERCIAL ARTISTS. Commercial artists, who may characterize themselves as commercial artists, commercial photographers, or	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[no comments received]</i>	(3) COMMERCIAL ARTISTS AND DESIGNERS. <i>[same as staff's]</i>

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2Action Item *	Regulatory Language Proposed by Staff	Regulatory Language Proposed by Guild (Alternative 1)	Regulatory Language Proposed by Blonder (Alternative 2)	Regulatory Language Proposed by Wayne (Alternative 3)	Regulatory Language Proposed by Liao (Alternative 4)	Regulatory Language Proposed by AAAA (Alternative 5)
	designers, provide services and tangible personal property to their clients for use in their clients' advertising campaigns, or for their clients' other commercial endeavors such as sales of copies of finished art (including, e.g., photographic images) provided by a commercial artist. Services they provide to their clients include the creation and development of ideas, concepts, looks, or messages. Electronic artwork they provide may be transferred through remote telecommunications such as by modem or over the Internet, or by tangible means through electronic media such as compact or floppy disc. Tangible personal property they provide may include electronic media on which electronic artwork is transferred to the client, hard copies of the electronic artwork, hard copies of finished art (which may consist of photographic images).					

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2Action Item *	Regulatory Language Proposed by Staff	Regulatory Language Proposed by Guild (Alternative 1)	Regulatory Language Proposed by Blonder (Alternative 2)	Regulatory Language Proposed by Wayne (Alternative 3)	Regulatory Language Proposed by Liao (Alternative 4)	Regulatory Language Proposed by AAAA (Alternative 5)
ACTION 4 – Definition of Contract of Sale	(4) CONTRACT OF SALE. An agreement to transfer tangible personal property for consideration is a contract of sale. A contract of sale consists of all terms comprising the obligation of the parties for the sale and purchase of the tangible personal property in question. A contract of sale may consist of a single contract document. A contract of sale may also consist of multiple documents. For example, a master agreement between an advertising agency and its client may specify the obligations of each with respect to the design of an advertising campaign for the client, the placement of the advertising with print and television media, and for the sale and purchase of tangible personal property related to the advertising campaign. There may then be additional terms for the purchase of specific tangible personal property during the advertising campaign, such as in a purchase order, which identifies the	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[no comments received]</i>	(4) CONTRACT OF SALE. An agreement to transfer tangible personal property for consideration is a contract of sale. A contract of sale consists of all terms comprising the obligation of the parties for the sale and purchase of the tangible personal property in question. A contract of sale may consist of a single contract document. A contract of sale may also consist of multiple documents. For example, a master agreement between an advertising agency and its client may specify the obligations of each with respect to the design of an advertising campaign for the client, the placement of the advertising with print and television media, and for the sale and purchase of tangible personal property related to the advertising campaign. There may then be additional terms for the purchase of specific tangible personal property during the advertising campaign, such as in a purchase order, which identifies the

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2Action Item *	Regulatory Language Proposed by Staff	Regulatory Language Proposed by Guild (Alternative 1)	Regulatory Language Proposed by Blonder (Alternative 2)	Regulatory Language Proposed by Wayne (Alternative 3)	Regulatory Language Proposed by Liao (Alternative 4)	Regulatory Language Proposed by AAAA (Alternative 5)
ACTION 3 – New Clarifying Language (Definition of Digital Pre- Press Instruction)	specific property that will be purchased and sold and the sales price for that property. In this example, not all terms of the sale and purchase of the tangible personal property identified in the purchase order are included in the master agreement, nor are all terms included in the purchase order. Rather, the contract of sale in this circumstance consists of the relevant provisions of the master agreement as modified by the specific provisions in the purchase order. <u>(5) DIGITAL PRE-PRESS INSTRUCTION. Digital pre-press instruction is the creation of original information in electronic form by combining more than one computer program into specific instructions or information necessary to prepare and link files for electronic transmission for output to film, plate, or direct to press, which is then transferred on electronic media such as tape or compact disc.</u>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	specific property that will be purchased and sold and the sales price for that property. In this example, not all terms of the sale and purchase of the tangible personal property identified in the purchase order are included in the master agreement, nor are all terms included in the purchase order. Rather, the contract of sale in this circumstance consists of the relevant provisions of the master agreement as modified by the specific provisions in the purchase order. <i>[no comments received – staff added language after final interested parties submissions were received]</i>

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2Action Item *	Regulatory Language Proposed by Staff	Regulatory Language Proposed by Guild (Alternative 1)	Regulatory Language Proposed by Blonder (Alternative 2)	Regulatory Language Proposed by Wayne (Alternative 3)	Regulatory Language Proposed by Liao (Alternative 4)	Regulatory Language Proposed by AAAA (Alternative 5)
ACTION 21 – General Language Differences	(6) ELECTRONIC ARTWORK. Electronic artwork is artwork created through the use of computer hardware and software processes which results in artwork in a digital format that can be transmitted to others via electronic means (that is, transmitted through remote telecommunications such as by modem or over the Internet, or by electronic media such as compact or floppy disc). Elements of the process include the creation of original artwork or photographic images, scanning of artwork or photographic images, composition and design of text, insertion and manipulation of scanned and original electronic artwork, photographic images, and text. Electronic artwork does not include artwork that is transferred to	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[no comments received]</i>	(5) ELECTRONIC ARTWORK. Electronic artwork is artwork created through the use of computer hardware and software processes which results in artwork in a digital format that can be transmitted to others the client or a third party via electronic means (that is, transmitted through remote telecommunications such as by modem or over the Internet, or by electronic media such as compact or floppy disc). Elements of the process include the creation of original artwork or photographic images, scanning of artwork or photographic images, composition and design of text, insertion and manipulation of scanned and original electronic artwork, photographic images, and text. Electronic artwork does not include artwork that is transferred to
ACTION 21 – General Language Differences	clients in a tangible form, other than on electronic media, even where such artwork may have been manufactured or produced in whole or in part by computer hardware and					customers in a tangible form, such as compact or floppy disc. other than on electronic media, even where such artwork may have been manufactured

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2Action Item *	Regulatory Language Proposed by Staff	Regulatory Language Proposed by Guild (Alternative 1)	Regulatory Language Proposed by Blonder (Alternative 2)	Regulatory Language Proposed by Wayne (Alternative 3)	Regulatory Language Proposed by Liao (Alternative 4)	Regulatory Language Proposed by AAAA (Alternative 5)
ACTION 6 - Definition of Intermediate Production Aids	(9) INTERMEDIATE PRODUCTION AIDS. Intermediate production aids include items such as artwork, illustrations, photograph images, photo engravings, and other similar materials which are used to produce special printing aids or other intermediate production aids. [Interested parties have indicated concurrence with staff's proposed language for subdivision (a)(10) – see Exhibit 5, page 2.]	[same as staff's]	[same as staff's]	(9) INTERMEDIATE PRODUCTION AIDS. Intermediate production aids include items such as artwork, illustrations, photograph images, photo engravings, and other similar materials which are used to produce finished art or other intermediate production aids.	[no comments received]	(8) INTERMEDIATE PRODUCTION AIDS. Intermediate production aids include items such as artwork, clip-art (pre- packaged art), illustrations, photograph images, photo engravings, and other similar materials which are used to produce special printing aids or other intermediate production aids.
ACTION 7 – Definition of Preliminary Art	(11) PRELIMINARY ART. Preliminary art is tangible personal property which is prepared solely for the purpose of demonstrating an idea or message for acceptance by the client before a contract is entered into or before approval is given for preparation of finished art to be furnished or licensed by the seller to his or her client, provided neither title to nor permanent possession of such tangible personal	[same as staff's]	[same as staff's]	(11) PRELIMINARY ART. Preliminary art is tangible personal property which is prepared solely for the purpose of demonstrating an idea or message for acceptance by the client before approval is given for preparation of finished art to be furnished or licensed by the seller to his or her client. The term “Preliminary art” implies that the same business entity that prepared the preliminary art,	[no comments received]	(10) PRELIMINARY ART. Preliminary art is tangible personal property which is prepared solely for the purpose of demonstrating an idea or message for acceptance by the client before a contract is entered into or before approval is given for preparation of finished art to be furnished or licensed by the seller to his or her client, provided neither title to nor permanent possession of such tangible personal property passes to the

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2Action Item *	Regulatory Language Proposed by Staff	Regulatory Language Proposed by Guild (Alternative 1)	Regulatory Language Proposed by Blonder (Alternative 2)	Regulatory Language Proposed by Wayne (Alternative 3)	Regulatory Language Proposed by Liao (Alternative 4)	Regulatory Language Proposed by AAAA (Alternative 5)
	<p>property passes to the client. Preliminary art may include roughs, visualizations, layouts, comprehensives, and instant photos.</p> <p><i>[Interested parties have indicated concurrence with staff's proposed language for subdivision (a)(12) – see Exhibit 5, page 3.]</i></p>			<p>subsequently prepared finished art based on the approved preliminary art. Preliminary art may include roughs, visualizations, layouts, comprehensives, and instant photos.</p>		<p>client. Preliminary art consists of creative art services whose object is to convey ideas for review by the client and as such, any tangible personal property, is incidental to the true object of the transaction. Preliminary art may include, but is not limited to, roughs, visualizations, layouts, comprehensives, and instant photos. Preliminary art is not subject to tax.</p>
ACTION 3 – New Clarifying Language (Definition of Third Parties)	<p><u>(13) THIRD PARTIES. A reference in this regulation to a transfer to a client also includes a transfer to a third party on the client's behalf. For example, the discussion in subdivision (b)(2)(B) for transfers of finished art by loading into the client's computer also includes transfers of the finished art by loading it into a third party's computer at the instruction of the client.</u></p>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[same as staff's]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>

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	<p>client title or the right to permanent possession of the artwork in tangible form, such as on electronic media or hard copy, or permanent possession of the artwork in tangible form is, in fact, transferred to the client.</p> <p>However, if the master agreement provides that the client owns the concepts embodied in</p>			<p>scope of the project is to provide consulting services only. The true intent of these services is to gain client approval to proceed with the preparation of finished art or, to provide nontaxable intangible consulting services. If the object of the job is to provide finished art and no approval is secured and no finished art was prepared, then these services are construed to be part of a “killed job” wherein no final product was produced and they are not taxable. Any tangible personal property produced is incidental to providing the service.</p> <p>However, if the master agreement provides that the client owns the concepts embodied in</p>		<p>incidental to the service provided and not subject to tax. However, if the master agreement provides that the advertising agency, artist or designer will pass to the client title or the right to permanent possession of the artwork in tangible form such as electronic media, or hard copy or permanent possession of the artwork in tangible form is in fact, transferred to the client, then tax is applicable. they are nontaxable unless the master agreement or other contract provides that the advertising agency or commercial artist will pass to the client title or the right to permanent possession of the artwork in tangible form, such as on electronic media or hard copy, or permanent possession of the artwork in tangible form is, in fact, transferred to the client</p> <p>However If the contract master agreement provides that the client owns the concepts</p>

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	tangible personal property that is owned and possessed by the advertising agency or commercial artist (e.g., so that such concepts cannot be used on behalf of any other person), that contract provision does not constitute the passage of title to tangible personal property to the client, provided the client does not thereby obtain the actual title to, or permanent possession of, the tangible personal property embodying the concepts and no other contractual provision passes such title to, or permanent possession of, such tangible personal property. A requirement that an advertising agency or commercial artist retain permanent possession of the artwork in tangible form does not itself constitute a sale of that property to the client in the absence of a provision passing title to such property to the client.			tangible personal property that is owned and possessed by the advertising agency or commercial artist (e.g., so that such concepts cannot be used on behalf of any other person), that contract provision does not constitute the passage of title to tangible personal property to the client.		embodied in tangible personal property that is owned and possessed by the advertising agency or commercial artist (e.g., so that such concepts cannot be used on behalf of any other person), that contract master agreement provision does not constitute the passage of title to tangible personal property to the client, provided the client does not thereby obtain the actual title to, or permanent possession of, the tangible personal property embodying the concepts. A requirement that an advertising agency or commercial artist retain permanent possession of the artwork in tangible form does not itself constitute a sale of that property to the client. in the absence of a provision passing title to such property to the client.

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ACTION 8 – Application of Tax to Services – Passage of Title (continued)	<p>(b)(1)(A) 2. Tangible personal property developed and used during services performed to convey ideas, concepts, looks, or messages is consumed in the performance of those services. Unless, prior to any use, the advertising agency or commercial artist passes title to such property to the client as discussed in the previous paragraph,</p> <p>the advertising agency or commercial artist is the consumer of such tangible personal property used and tax applies to the sale of property to, or to the use of the property by, the advertising agency or commercial artist. If the advertising agency or commercial artist passes title to, or permanent possession of, such tangible personal property to its client, tax applies to the sale of the tangible personal property by the advertising agency or commercial artist to the client.</p>	<p>(b)(1)(A) [same as staff's]</p>	<p>(b)(1)(A) [same as staff's]</p>	<p>(b)(1)(A) 2. Tangible personal property developed and used during services performed to convey ideas, concepts, looks, or messages is consumed in the performance of those services. Unless, prior to any use, the advertising agency or commercial artist, acting as a retailer, passes title to such property to the client by means of a title clause in the contract of sale that passes title to the client prior to use, the advertising agency or commercial artist is the consumer of such tangible personal property used and tax applies to the sale of property to, or to the use of the property by, the advertising agency or commercial artist. If the advertising agency or commercial artist passes title to, or permanent possession of, such tangible personal property to its client, tax applies to the sale of the tangible personal property by the advertising agency or commercial artist to the client.</p>	<p>(b)(1)(A) [no comments received]</p>	<p>(c)(1)(A) [same as staff's]</p>

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<p>ACTION 3 – New Clarifying Language (Digital Pre-Press Instruction)</p> <p>(b)(1) (B) Digital Pre-Press Instruction. <u>Digital pre-press instruction is a custom computer program under section 6010.9 of the Revenue and Taxation Code, the sale of which is not subject to tax, provided the digital pre-press instruction is prepared to the special order of the purchaser.</u></p>	<p>(b)(1) (B) Digital Pre-Press Instruction. <u>Digital pre-press instruction is a custom computer program under section 6010.9 of the Revenue and Taxation Code, the sale of which is not subject to tax, provided the digital pre-press instruction is prepared to the special order of the purchaser.</u></p>	<p>(b)(1) <i>[no comments received – staff added language after final interested parties submissions were received]</i></p>	<p>(b)(1) <i>[no comments received – staff added language after final interested parties submissions were received]</i></p>	<p>(b)(1) <i>[no comments received – staff added language after final interested parties submissions were received]</i></p>	<p>(b)(1) <i>[no comments received – staff added language after final interested parties submissions were received]</i></p>	<p>(c)(1) (B) Digital Pre-Press Instruction. A file prepared to the special order of the client which qualifies as digital pre-press instruction as defined in subdivision (f) of Regulation 1541 is a custom computer program, and its transfer is not subject to tax regardless of the form in which the file is transferred or the time at which it is transferred. Electronic or digital pre-press instruction shall not, however, be regarded as a custom computer program if it is a "canned" or prewritten computer program which is held or existing for general or repeated sale or lease, even if the electronic or digital pre-press instruction was initially developed on a custom basis or for in-house use. In such cases, the "canned" software is taxable.</p>
<p>ACTION 21 – General Language Differences [Alternative 5]</p>	<p><u>Digital pre-press instruction shall not, however, be regarded as a custom computer program if it is a "canned" or prewritten computer program which is held or existing for general or repeated sale or lease, even if the digital pre-press instruction was initially developed on a custom basis or for in-house use. The sale of such canned or prewritten digital pre-press instruction in tangible form is a sale of tangible personal property, the retail sale of which is subject to tax.</u></p>					

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	<i>[Interested parties have indicated concurrence with staff's proposed language for subdivision (b)(1)(C) through (b)(1)(E)– see Exhibit 5, page 4.]</i>					
ACTION 21 – General Language Differences [Alternative 5]	(b)(1) (F) Specific Nontaxable Charges. The following and similar fees and commissions are not taxable when they are separately stated. Whether separately stated or not, these fees and commissions are not included in the calculation of “direct labor” for purposes of subdivision (b)(3).	(b)(1) <i>[same as staff's]</i>	(b)(1) <i>[same as staff's]</i>	(b)(1) (F) Specific Nontaxable Charges. The following and similar fees and commissions are not taxable when they are separately stated. Whether separately stated or not, these fees and commissions are considered to be markup for purposes of subdivision (b)(3).	(b)(1) <i>[no comments received]</i>	(c)(1) (F) Specific Nontaxable Charges. The following , and similar fees and commissions are not taxable when they are separately stated. Whether separately stated or not, these fees and commissions are not included in the calculation of “direct labor” for purposes of subdivision (b)(3).
ACTION 9 – Specific Nontaxable charges [Alternative 3]				(1) Agent fees added to purchases of tangible personal property by agencies established as agents for their clients as compensation for their performances of services related to such purchases		
ACTION 21 – General Language Differences	(b)(1)(F) 1. Media commissions received for placement of	<i>[same as staff's]</i>	<i>[same as staff's]</i>	(b)(1)(F) <i>[Subsequent commissions and fees would be</i>	<i>[no comments received]</i>	(c)(1)(F) 1. Media commissions or fees received for

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	advertising whether paid by the medium, by another advertising agency, or by the client. 2. Commissions paid to advertising agencies by suppliers. Examples of such commissions are those paid to an advertising agency by a premium manufacturer (or distributor) or a direct-by-mail supplier. <i>[Interested parties have indicated concurrence with staff's proposed language for subdivision (b)(1)(F)3. through (F)6. – see Exhibit 5, page 5.]</i>			<i>renumbered 2 through 7 - otherwise same as staff's]</i>		placement of advertising whether paid by the medium, by another advertising agency, or by the client. 2. Commissions or fees paid to advertising agencies by suppliers. Examples of such commissions are those paid to an advertising agency by a premium manufacturer (or distributor) or a direct-by-mail supplier.
ACTION 3 - New Clarifying Language (Example for Application of Tax)	<u>(b)(1)</u> <u>(G) Example. A designer contracts to create and sell printed brochures to a law firm. The contract separately states a charge for design, for art direction, for preliminary art, and for the printed brochures. The designer's design and art direction services culminate in the creation of preliminary art that the designer uses to show the</u>	<i>[same as staff's]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>

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	<p><u>designer's concepts to the law firm. After the law firm approves the concepts, the designer finalizes the design of the brochure and contracts with a printer to print the brochures. The printer sells the printed brochures to the designer for resale, and the designer resells the printed brochures to the law firm. The only tangible personal property that will be transferred to the law firm (or to anyone on behalf of the law firm) are the printed brochures. The law firm will not obtain title to, or the right to possession of, any finished art or any other tangible personal property. Tax does not apply to the designer's separately stated charges for design, art direction, and preliminary art. Tax applies to the designer's separately stated charge to the law firm for the printed brochures.</u></p> <p><i>[Interested parties have indicated concurrence with staff's proposed language for subdivision (b)(2)(A) – see Exhibit 5, page 5.]</i></p>					

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ACTION 10 – Use of Aids in Creation of Finished Art – Title Clause Agreement	<p><u>(b)(2) FINISHED ART.</u></p> <p>(A) Use of Aids in Creation of Finished Art.</p> <p>No subdivision recommended.</p>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<p>(c)(2) FINISHED ART.</p> <p>(A) Use of Aids in Creation of Finished Art.</p> <p>(1) Prior to the preparation of finished art, if the client signs a title clause agreement to purchase intermediate production aids or obtain the lease rights for illustrations, electronic art, photography, typography, airbrushing, photo retouching, filmwork, photostats, dies, lithographic film and plates, photo engravings, and other materials needed to prepare the finished artwork, the intermediate production aids are taxed only once.</p>
ACTION 21– General Language Differences	<p>(b)(2) (B) Transfers of Finished Art Not in Tangible Form.</p> <p>A transfer of electronic artwork from an advertising agency or commercial artist to the client or to a third party</p>	<p>(b)(2) <i>[same as staff's]</i></p>	<p>(b)(2) <i>[same as staff's]</i></p>	<p>(b)(2) <i>[same as staff's]</i></p>	<p>(b)(2) <i>[no comments received]</i></p>	<p>(c)(2) (B) Transfers of Finished Art Not in Tangible Form. (Electronic Artwork). A transfer of electronic artwork from an advertising agency or commercial artist to the client or to a third party</p>

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	on the client's behalf that is not in tangible form is not a sale of tangible personal property, and the charges for the transfer are not subject to tax. A transfer of electronic artwork is not in tangible form if the file containing the electronic artwork is transferred through remote telecommunications (such as by modem or over the Internet), or if the file is loaded into the client's computer by the advertising agency or commercial artist, and the client does not obtain title to or possession of any tangible personal property, such as electronic media or hard copy. If the transfer is not a transfer in tangible form because it is loaded onto the client's computer, the advertising agency or commercial artist should document that transfer by a written statement signed at the time of loading by the client and by the person who loaded the electronic artwork into the client's computer with the following or similar language: "This electronic					on the client's behalf that is not in tangible form is not a sale of tangible personal property, and the charges for the transfer are not subject to tax. A transfer of electronic artwork is not in tangible form if the file containing the electronic artwork is transferred through remote telecommunications (such as by modem or over the Internet), or if the file is loaded into the client's computer by the advertising agency or commercial artist, and the client does not obtain title to or possession of any tangible personal property, such as electronic media or hard copy. If the transfer is not a transfer in tangible form because it is loaded onto the client's computer, the advertising agency or commercial artist should document that transfer by a written statement signed at the time of loading by the client and by the person who loaded the electronic artwork into the client's computer with the following or similar language: "This electronic

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ACTION 21 – General Language Differences	<p>artwork was loaded into the computer of [client's name] by [seller's name], and [seller's name] did not transfer any tangible personal property containing the artwork, such as electronic media or hard copies, to [client's name].”</p> <p>When such a statement is signed at the time the file is loaded,</p> <p>it will be rebuttably presumed that the transfer of electronic artwork was not transferred in tangible form. If there is no such timely completed statement, the advertising agency or commercial artist may provide other substantive evidence establishing that the artwork was not transferred in tangible form.</p> <p>(b)(2) (C) Transfers of Finished Art in Tangible Form. The electronic or manual preparation of</p>	<p>(b)(2) [same as staff's]</p>	<p>(b)(2) [same as staff's]</p>	<p>(b)(2) (C) Transfers of Finished Art in Tangible Form. The electronic or manual preparation of</p>	<p>(b)(2) [no comments received]</p>	<p>artwork was loaded into the computer of [client's name] by [advertising agency, artist or designer's name] and [advertising agency, artist or designer's name] did not transfer any tangible personal property containing the artwork, such as electronic media or hard copies, to [client's name].” When such a statement is signed or initialed at the time the file is loaded or at the point the transfer is invoiced to the client, it will be rebuttably presumed that the transfer of electronic artwork was not transferred in tangible form. If there is no such timely completed statement, the advertising agency or commercial artist may provide other substantive evidence establishing that the artwork was not transferred in tangible form.</p> <p>(c)(2) (C) Transfers of Finished Art in Tangible Form. The electronic or manual preparation of</p>

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<p>ACTION 21 – General Language Differences</p> <p>ACTION 2 – Organization of Regulation [Created subdivision (b)(2)(C)1.]</p>	<p>finished art for use in reproduction or display is not a service. Unless the transfer is not in tangible form as explained in subdivision (b)(2)(B), the transfer of finished art is a sale of tangible personal property and tax applies to charges for that finished art, including all charges for any rights sold with the finished art, such as copyrights or distribution and production rights, except as provided in subdivision (b)(2)(D)2. If charges for finished art are combined into a single charge that also includes nontaxable charges for conceptual services described in subdivision (b)(1)(A), the advertising agency or commercial artist may report the measure of tax on the retail sale of the finished art as specified in subdivision (b)(3), provided that the reported measure of tax must also include the value of reproduction rights included with the transfer except those that are not taxable as provided in subdivision (b)(2)(D)2.</p>			<p>finished art for use in reproduction or display is not a service. Unless the transfer is not in tangible form as explained in subdivision (b)(2)(B), the transfer of finished art is a sale of tangible personal property and tax applies to charges for that finished art, including all charges for any rights sold with the finished art, such as copyrights or distribution and production rights, except as provided in subdivision (b)(2)(D)2. If charges for finished art are combined into a single charge that also includes nontaxable charges for conceptual services described in subdivision (b)(1)(A), the advertising agency or commercial artist may report the measure of tax on the retail sale of the finished art as specified in subdivision (b)(3), provided that the reported measure of tax must also include the value of reproduction rights included with the transfer except those that are not taxable as provided in subdivision (b)(2)(D)2.</p>		<p>finished art for use in reproduction or display is not a service. Unless the transfer is not in tangible form as explained in subdivision (b)(2)(B), The transfer of finished art in tangible form is a sale of tangible personal property and tax applies to charges for that finished art, including all charges for any rights sold with the finished art such as copyrights or distribution and production rights, except as provided in subdivision (b)(2)(D)2. If charges for finished art are combined into a single charge that also includes nontaxable charges for conceptual services described in subdivision (b)(1)(A), the advertising agency or commercial artist may report the measure of tax on the retail sale of the finished art as specified in subdivision (b)(3), provided that the reported measure of tax must also include the value of reproduction rights included with the transfer except those that are not taxable as provided in subdivision (b)(2)(D)2.</p>

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	<p>If tax is not reported on this basis, it will be rebuttably presumed that 75 percent of the combined charge for the finished art and conceptual services is for the nontaxable services and that 25 percent of the combined charge is the measure of tax on the retail sale of the finished art, provided that 25 percent of the combined charge is not less than the sales price to the advertising agency or commercial artist of the finished art (or component parts) and any intermediate production aids or special printing aids sold to the client for that combined charge.</p>			<p>If tax is not reported on this basis, it will be rebuttably presumed that 75 percent of the combined charge for the finished art and conceptual services is for the nontaxable services and that 25 percent of the combined charge is the measure of tax on the retail sale of the finished art, provided that 25 percent of the combined charge is not less than the sales price to the advertising agency or commercial artist of the finished art (or component parts) and any intermediate production aids or special printing aids sold to the client for that combined charge.</p>		<p>1. Lump sum billing of in-house artwork containing preliminary art and finished art.</p> <p>An advertising agency, artist or designer may elect to do a lump-sum billing of in-house artwork containing both preliminary art and finished art. If tax is not reported on this basis, On billing of in-house artwork for which an advertising agency, artist or designer makes a lump-sum charge that includes both preliminary art and other nontaxable services and finished art, it will be rebuttably presumed that 75 percent of the combined charge for the finished art and conceptual services is for the nontaxable services and that 25 percent of the combined charge is the measure of tax on the retail sale of the finished art, provided that 25 percent of the combined charge is not less than the sales price to the advertising agency or commercial artist of the finished art (or</p>

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ACTION 11 – Transfers of Finished Art in Tangible Form – Cost of Special Printing Aids	If such sales price to the advertising agency or commercial artist is more than 25 percent of the combined charge to the client, the measure of tax shall be deemed to be such sales price of the tangible personal property to the advertising agency or commercial artist.	<i>[same as staff's]</i>	<i>[same as staff's]</i>	If such sales price to the advertising agency or commercial artist is more than 25 percent of the combined charge to the client, the measure of tax shall be deemed to be such sales price of the tangible personal property to the advertising agency or commercial artist.	<i>[no comments received in response to staff's revised language]</i>	component parts) and any intermediate production aids or special printing aids sold to the client for that combined charge. If such sales price to the advertising agency or commercial artist is more than 25 percent of the combined charge to the client, the measure of tax shall be deemed to be such sales price of the tangible personal property to the advertising agency or commercial artist.
ACTION 12 – Transfers of Finished Art in Tangible Form – Option to Separately State Special Printing Aids				Intermediate production aids or special printing aids sold to the client that are separately listed and priced on the invoice to the client are subject to the rules governing an advertising agency acting as an agent or retailer as described in subdivision (c).		
ACTION 13 – Technology Transfer Agreement – Requirement That It Be in Writing	(b)(2) (D) Reproduction Rights Transferred With Finished Art. 2. Any agreement evidenced by a writing (such as a contract, invoice, or purchase	(b)(2) (D) Reproduction Rights Transferred With Finished Art. 2. Any agreement evidenced by a writing (such as a contract, invoice, or purchase	(b)(2) <i>[same as staff's]</i>	(b)(2) <i>[same as staff's]</i>	(b)(2) (D) Reproduction Rights Transferred With Finished Art. 2. Any agreement that assigns or licenses a copyright interest in finished art for the	(c)(2) <i>[same as staff's]</i>

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ACTION 14 – Technology Transfer Agreement - Finished Art Transferred on Computer Storage Media	<p>order) that assigns or licenses a copyright interest in finished art for the purpose of reproducing and selling other property subject to the copyright interest is a technology transfer agreement, as explained further in Regulation 1507. Tax applies to amounts received for any tangible personal property transferred as part of a technology transfer agreement.</p> <p>Tax does not apply to amounts received for the assignment or licensing of a copyright interest as part of a technology transfer agreement. The measure of tax on the sale of finished art transferred by an advertising agency or commercial artist as part of a technology transfer agreement shall be:</p>	<p>order) that assigns or licenses a copyright interest in finished art for the purpose of reproducing and selling other property subject to the copyright interest is a technology transfer agreement, as explained further in Regulation 1507. Tax applies to amounts received for any tangible personal property transferred as part of a technology transfer agreement.</p> <p>Notwithstanding subdivision (b)(2)(B), tax does not apply to temporary transfers of computer storage media containing finished art transferred as part of a technology transfer agreement.</p> <p>Tax does not apply to amounts received for the assignment of a copyright interest to a third party as part of a technology transfer agreement. The measure of tax on the sale of finished art transferred by an advertising agency or commercial artist as part of a technology transfer agreement shall be:</p>			<p>purpose of reproducing and selling other property subject to the copyright interest is a technology transfer agreement, as explained further in Regulation 1507. Tax applies to amounts received for any tangible personal property transferred as part of a technology transfer agreement.</p> <p>Tax does not apply to amounts received for the assignment or licensing of a copyright interest as part of a technology transfer agreement. The measure of tax on the sale of finished art transferred by an advertising agency or commercial artist as part of a technology transfer agreement shall be:</p>	

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ACTION 21 – General Language Differences [Alternative 2]	(b)(2)(D)2 a. The separately stated sales price for the finished art, provided the separately stated price represents a fair market value of the tangible personal property;	(b)(2)(D)2 a. The separately stated sales price for the finished art, provided the separately stated price is reasonable ;	(b)(2)(D)2 a. The separately stated sales price for the finished art, provided the separately stated price represents either (i) the fair market value of the tangible personal property; or (ii) if the possession of the finished art is transferred temporarily for purposes of reproduction, the fair rental value of the tangible personal property ;	(b)(2)(D)2 a. <i>[same as staff's]</i>	(b)(2)(D)2 a. <i>[same as staff's]</i>	(c)(2)(D)2 a. <i>[same as staff's]</i>
ACTION 15 Technology Transfer Agreement – Separately Stated Price						
ACTION 3 - New Clarifying Language (Finished Art and Like Finished Art)	b. Where there is no such separately stated price, the separate price at which the person holding the copyright interest in the finished art has sold or leased <u>that finished art or</u> <u>like finished art to an</u> <u>unrelated third party</u> where: 1) the finished art <u>was sold or leased</u> <u>without also transferring</u> <u>an interest in the</u> <u>copyright</u> ; or 2) the <u>finished art was sold or</u> <u>leased in another</u> <u>transaction at a stated</u> <u>price satisfying the</u> <u>requirements of</u> <u>subdivisions</u> (b)(2)(D)2.a.; or	<i>[same as staff's]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>

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AGENDA D – February 5, 2002 Business Taxes Committee Meeting
Graphic Arts and Related Enterprises – Regulation 1540, Advertising Agencies,
Commercial Artists and Designers

2Action Item *	Regulatory Language Proposed by Staff	Regulatory Language Proposed by Guild (Alternative 1)	Regulatory Language Proposed by Blonder (Alternative 2)	Regulatory Language Proposed by Wayne (Alternative 3)	Regulatory Language Proposed by Liao (Alternative 4)	Regulatory Language Proposed by AAAA (Alternative 5)
<p>ACTION 17 – Cost of Materials – Includes Those Used as Well as Incorporated [Alternative 4]</p> <p>ACTION 16 – Technology Transfer Agreement – the Value of the Artist’s Labor [Alternative 1 and 2]</p>	<p>c. If there is no such separately stated price under subdivision (b)(2)(D)2.a., nor a separate price under subdivision (b)(2)(D)2.b., 200 percent of the combined cost of materials and labor used to produce or acquire the finished art. “Cost of materials” consists of the costs of those materials used or incorporated into the finished art, or any tangible personal property transferred as part of the technology transfer agreement. “Labor” includes any charges or value of labor used to create such tangible personal property whether the advertising agency or commercial artist performs such labor, a third party performs the labor, or the labor is performed through some combination thereof. The value of labor provided by the advertising agency or commercial artist shall equal the lower of the normal and customary charges for labor billed to third parties by the advertising agency or</p>	<p>c. If there is no such separately stated price under subdivision (b)(2)(D)2.a., nor a separate price under subdivision (b)(2)(D)2.b., 200 percent of the combined cost of materials and labor used to produce or acquire the finished art. “Cost of materials” consists of the costs of those materials used or incorporated into the finished art, or any tangible personal property transferred as part of the technology transfer agreement. “Labor” means any charges for labor used to create such tangible personal property where the advertising agency or commercial artist purchases such labor from a third party or the work is performed by an employee of the advertising agency or commercial artist.</p>	<p>c. If there is no such separately stated price under subdivision (b)(2)(D)2.a., nor a separate price under subdivision (b)(2)(D)2.b., 200 percent of the combined cost of materials and labor used to produce or acquire the finished art. “Cost of materials” consists of the costs of those materials used or incorporated into the finished art, or any tangible personal property transferred as part of the technology transfer agreement. “Cost of labor” includes any consideration paid to an employee or an independent contractor for labor used to create such tangible personal property.</p>	<p>[same as staff’s]</p>	<p>c. If there is no such separately stated price under subdivision (b)(2)(D)2.a., nor a separate price under subdivision (b)(2)(D)2.b., 200 percent of the combined cost of materials and labor used to produce or acquire the finished art. “Cost of materials” consists of the costs of those materials physically incorporated into the finished art, or any tangible personal property transferred as part of the technology transfer agreement. “Labor” includes any charges or value of labor used to create such tangible personal property whether the advertising agency or commercial artist performs such labor, a third party performs the labor, or the labor is performed through some combination thereof. The value of labor provided by the advertising agency or commercial artist shall equal the lower of the normal and customary charges for labor billed to third parties by the advertising agency or</p>	<p>c. If there is no such separately stated price under subdivision (b)(2)(D)2.a., nor a separate price under subdivision (b)(2)(D)2.b., 200 percent of the combined cost of materials and labor used to produce or acquire the finished art. “Cost of materials” consists of the costs of those materials used or incorporated into the finished art, or any tangible personal property transferred as part of the technology transfer agreement. “Labor” includes any charges or value of labor used to create such tangible personal property whether the advertising agency or commercial artist performs such labor, a third party performs the labor, or the labor is performed through some combination thereof. The value of labor provided by the advertising agency or commercial artist shall equal the lower of the normal and customary charges for labor billed to third parties by the advertising agency or</p>

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AGENDA D – February 5, 2002 Business Taxes Committee Meeting
Graphic Arts and Related Enterprises – Regulation 1540, Advertising Agencies,
Commercial Artists and Designers

2Action Item *	Regulatory Language Proposed by Staff	Regulatory Language Proposed by Guild (Alternative 1)	Regulatory Language Proposed by Blonder (Alternative 2)	Regulatory Language Proposed by Wayne (Alternative 3)	Regulatory Language Proposed by Liao (Alternative 4)	Regulatory Language Proposed by AAAA (Alternative 5)
<p>ACTION 21 – General Language Differences [Alternative 5]</p> <p>ACTION 16 – Technology Transfer Agreement – the Value of the Artist’s Labor (continued)</p> <p>ACTION 18 – Explanation of Calculation of Sales Price of Other Tangible Personal Property</p>	<p>commercial artist, or the fair market value of the labor performed by the advertising agency or commercial artist.</p> <p>(b)(3) SALES OF OTHER TANGIBLE PERSONAL PROPERTY BY ADVERTISING AGENCY OR COMMERCIAL ARTIST. Tax applies to the total charge for the retail sale of tangible personal property by an advertising agency or commercial artist. If an advertising agency or commercial artist combines charges for nontaxable services as defined in subdivision</p>	<p><i>[If staff’s recommendation is adopted, the Guild proposes the following language be added as the last sentence of the paragraph.]</i></p> <p>In the absence of evidence of a price charged by that commercial artist or advertising agency for labor only, the fair market value for such labor shall be presumed to be \$100.</p> <p>(b)(3) <i>[same as staff’s]</i></p>	<p>(b)(3) <i>[same as staff’s]</i></p>	<p>(b)(3) <i>[same as staff’s]</i></p>	<p>commercial artist, or the fair market value of the labor performed by the advertising agency or commercial artist.</p> <p>(b)(3) <i>[no comments received]</i></p>	<p>commercial artist, or the fair market value of the labor performed by the advertising agency or commercial artist.</p> <p>Nontaxable fees, charges and commissions are not included in the calculation of direct labor (see (c) (1) (f).</p> <p>(b)(3) SALES OF OTHER TANGIBLE PERSONAL PROPERTY BY ADVERTISING AGENCY OR COMMERCIAL ARTIST. Tax applies to the total charge for the retail sale of tangible personal property by an advertising agency or commercial artist. If an advertising agency or commercial artist combines charges for nontaxable services as defined in subdivision</p>

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	(b)(1)(F), such as media placement, with charges for tangible personal property for which the advertising agency or commercial artist is the retailer, the measure of tax on that retail sale of property includes the total of: direct labor; the cost of purchased items that become an ingredient or component part of the tangible personal property; the cost of any intermediate production aids or special printing aids; and a reasonable markup. Commissions, fees, and other charges exclusively related to the production or fabrication of tangible personal property are part of direct labor and are thus included in the measure of tax. Such charges include retouching of photographic images or other artwork for reproduction, provided the retouching is intended to improve the quality of the reproduction. An advertising agency or commercial artist must keep sufficient records to document the basis for the reported measure of tax.					(b)(1)(F), such as media placement, with charges for tangible personal property for which the advertising agency or commercial artist is the retailer, the measure of tax on that retail sale of property includes the total of: direct labor; the cost of purchased items that become an ingredient or component part of the tangible personal property; the cost of any intermediate production aids or special printing aids; and a reasonable markup. Commissions, fees, and other charges exclusively related to the production or fabrication of tangible personal property are part of direct labor and are thus included in the measure of tax. Such charges include retouching of photographic images or other artwork for reproduction, provided the retouching is intended to improve the quality of the reproduction. An advertising agency or commercial artist must keep sufficient records to document the basis for the reported measure of tax.

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Graphic Arts and Related Enterprises – Regulation 1540, Advertising Agencies,
Commercial Artists and Designers

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ACTION 21 – General Language Differences	(b)(4) ITEMS PURCHASED BY AN ADVERTISING AGENCY OR COMMERCIAL ARTIST. Except when property is resold prior to any use, an advertising agency or commercial artist is the consumer of tangible personal property used in the operation of its business. Tax applies to the sale of such property to, or to the use of such property by, the advertising agency or commercial artist.	(b)(4) [same as staff's]	(b)(4) [same as staff's]	(b)(4) [same as staff's]	(b)(4) [no comments received]	(b)(4) ITEMS PURCHASED BY AN ADVERTISING AGENCY OR COMMERCIAL ARTIST. Except when property is resold prior to any use, an advertising agency or commercial artist is the consumer of tangible personal property used in the operation of its business. Tax applies to the sale of such property to, or to the use of such property by, the advertising agency or commercial artist.
	(c) SITUATIONS SPECIFIC TO ADVERTISING AGENCIES. (1) ADVERTISING AGENCY ACTING AS AN AGENT FOR ITS CLIENT. An agent is one who represents another, called the principal, in dealings with third persons. (Civil Code section 2295.) To the extent that an advertising agency acts as the agent of its client when acquiring tangible personal property, it is	[same as staff's]	[same as staff's]	[same as staff's]	[no comments received]	(b) SITUATIONS SPECIFIC TO ADVERTISING AGENCIES. (1) ADVERTISING AGENCY ACTING AS AN AGENT FOR ITS CLIENT. An agent is one who represents another, called the principal, in dealings with third persons. (Civil Code section 2295). To the extent that an advertising agency acts as the agent of its client when acquiring tangible personal property, it is

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ACTION 21 – General Language Differences	neither a purchaser of the property with respect to the supplier nor a seller of the property with respect to its principal (that is, its client). Because of the unique relationship between advertising agencies and their clients, unless an advertising agency elects non-agent status under subdivision (c)(2)(A) or is otherwise the retailer of the property under subdivision (c)(2)(B) or (c)(2)(C), it is rebuttably presumed that the advertising agency acts as the agent of its client when acquiring tangible personal property on its client's behalf.					neither a purchaser of the property with respect to the supplier nor a seller of the property with respect to its principal (that is, its client). Because of the unique relationship between advertising agencies and their clients, unless the advertising agency elects non-agent status under subdivision (c)(2)(A), or is otherwise the retailer of the property under subdivision (c)(2)(B) or (c)(2)(C) it is rebuttably presumed that the advertising agency acts as an agent of its client when acquiring tangible personal property on its client's behalf. (See (c)(2)(A),(B),(C).
	(c)(1) (A) A supplier of tangible personal property to an advertising agency is presumed to have made a retail sale of that property unless the supplier takes a timely and valid resale certificate in good faith from the advertising agency. Otherwise, the supplier has the burden of establishing that the advertising agency	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[no comments received]</i>	(b)(1) (A) A supplier of tangible personal property to an advertising agency is presumed to have-made a retail sale of that property unless the supplier takes a timely and valid resale certificate in good faith from the advertising agency. Otherwise, the supplier has the burden of establishing that the advertising agency

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ACTION 21 – General Language Differences	<p>elected non-agent status under subdivision (c)(2)(A) and resold the property or that the advertising agency resold the property as the retailer under subdivision (c)(2)(B) or (c)(2)(C).</p> <p>(c)(1) <i>[Interested parties have indicated concurrence with staff's proposed language for subdivision (c)(1)(B) – see Exhibit 5, page 8.</i></p>					<p>elected non-agent status under subdivision (c)(2)(A) and resold the property or that the advertising agency resold the property as the retailer under subdivision (c)(2)(B) or (c)(2)(C).</p>
ACTION 19 – Evidence to Prove Erroneous Issuance of a Resale Certificate	<p>(c)(1) (C) An advertising agency may not issue a resale certificate when purchasing tangible personal property as the agent of its client. An advertising agency who issues a resale certificate to a supplier is presumed to be purchasing tangible personal property from that supplier on its own behalf for resale and not to be acting as an agent of its client. However, the advertising agency may provide evidence to prove that its issuance of the resale certificate was erroneous and that the advertising agency was</p>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[no comments received]</i>	<p>(b)(1) (C) An advertising agency may not issue a resale certificate when purchasing tangible personal property as the agent of its client. An advertising agency who issues a resale certificate to a supplier is presumed to be purchasing tangible personal property from that supplier on its own behalf for resale and is not to be acting as an agent of its client. However, the advertising agency may provide evidence to prove that its issuance of the resale certificate was erroneous and that the advertising</p>

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ACTION 19 – Evidence to Prove Erroneous Issuance of a Resale Certificate (continued)	acting as an agent of its client, provided the advertising agency has not treated the transaction as its own sale of tangible personal property to its client, collecting tax or tax reimbursement from its client on that sale. If the resale certificate was issued in error, the advertising agency is liable for use tax on the cost of tangible personal property purchased under the certificate unless the advertising agency has already paid that tax to the supplier or to the Board, or the client has self-reported and paid the tax to the Board.					agency was acting as an agent of its client; provided the advertising agency has not treated the transactions as its own sale of tangible personal property or its client, collecting tax or tax reimbursement from its client on that sale. If the resale certificate was issued in error, the advertising agency is liable for use tax on the cost of tangible personal property purchased under the certificate unless the advertising agency has already paid that tax to the supplier or to the Board, or the client has self-reported and paid the tax to the Board.
ACTION 3 - New Clarifying Language (Advertising Agency Acting as Retailer)	(c)(2) ADVERTISING AGENCY ACTING AS A RETAILER. An advertising agency that acts as a retailer of tangible personal property may issue a resale certificate for such tangible personal property if the property will be resold prior to any use. <u>Absent an agreement that the property will be sold prior to use, tax is due on the purchase price of</u>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[same as staff's]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>

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	<p><u>tangible personal property that is used prior to being resold to the client and, in addition, tax is also due on the sales price of the tangible personal property to the client.</u></p> <p>(A) Election of Non-Agent Status. An advertising agency may elect non-agent status with respect to sales of tangible personal property to its client. This election must be supported by a specific written statement in its master agreement with the client. Alternatively, a statement may be included on an advertising agency's job order or invoice to its client. Statements should include the following or similar language: “(Advertising Agency's name) will not be acting as an agent of (client's name) for purposes of this transaction.”</p> <p>An advertising agency that elects non-agent status is a retailer with respect to tangible personal property sold to its clients. The measure of tax on the advertising</p>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[no comments received]</i>	<p>(A) Election of Non-Agent Status. An advertising agency may elect non-agent status with respect to sales of tangible personal property to its client. This election must be supported by a specific written statement in its master agreement with the client. Alternatively, a statement may be included on an advertising agency's job order or invoice to its client. Statements should include the following or similar language: “(Advertising Agency's name) will not be acting as an agent of (client's name) for purposes of this transaction.”</p> <p>An advertising agency that elects non-agent status is a retailer with respect to tangible personal property sold to its clients. The measure of tax on the advertising</p>

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ACTION 21 – General Language Differences	agency's retail sale is the separately stated charge for the tangible personal property. If there is no such separately stated charge, the measure of tax is calculated as provided in subdivision (b).					agency's retail sale is the separately stated charge for the tangible personal property. If there is no such separately stated charge, the measure of tax is calculated as provided in subdivision (c).
	(c)(2) (B) Items Produced or Fabricated by an Advertising Agency in-House. Advertising agencies are retailers of tangible personal property they produce or fabricate, e.g., by their own employees. Advertising agencies are not agents of their clients with respect to the acquisition of materials incorporated into such items of tangible personal property they produce or fabricate,	(c)(2) <i>[same as staff's]</i>	(c)(2) <i>[same as staff's]</i>	(c)(2) (B) Items Produced or Fabricated by an Advertising Agency in-House. Advertising agencies are retailers of tangible personal property they produce or fabricate, e.g., by their own employees. Advertising agencies are not agents of their clients with respect to the acquisition of materials incorporated into such items of tangible personal property they produce or fabricate,	(c)(2) <i>[no comments received]</i>	Except for in-house artwork billed on a lump sum method under section (c)(5), tax is due on the taxable selling price of tangible personal property . If there is no separately stated charge, the taxable selling price may be calculated as shown in subdivision (c). (b)(2) (B) Items Produced or Fabricated by an Advertising Agency in-House. Advertising agencies are retailers of tangible personal property they produce or fabricate, e.g., by their own employees. Advertising agencies are not agents of their clients with respect to the acquisition of materials incorporated into such items of tangible personal property they produce or fabricate,

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ACTION 21 – General Language Differences [Alternative 3 and 5]	but instead are the retailers of such property. The measure of tax on their retail sale of that property is the separately stated charge for the property sold. If there is no such separately stated charge, the measure of tax is calculated as provided in subdivision (b).			but instead are the retailers of such property. The measure of tax on their retail sale of that property is the separately stated charge for the property sold. If there is no such separately stated charge, the measure of tax is calculated as provided in subdivision (b). The term “incorporated” means those items that become an ingredient or part of the property and not those that are merely consumed or used in the production of the property sold. For example, materials such as bronze in a sculpture or canvas in a painting are incorporated into the property and may not be treated as an agent transaction. A photograph is not incorporated into finished art if only a copy of the photograph was incorporated into the finished art and it may be treated as an agent transaction. (c)(1).		but instead are the retailers of such property. The measure of tax on their retail sale of that property is the separately stated charge for the property sold. If there is no such separately stated charge, the measure of tax is calculated as provided in subdivision (c). Except for in-house artwork billed as a lump-sum under section (c)(5), tax is due on the taxable selling price of tangible personal property fabricated or produced by the advertising agency's employees. In those situations, an advertising agency should issue a resale certificate when purchasing items that become part of such tangible personal property.

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ACTION 20 – Invoice to Client for More Than Cost of Property	(c)(2) (C) Invoice to Client for More Than Cost of Tangible Personal Property to Advertising Agency. When an advertising agency invoices its client for tangible personal property provided by the advertising agency without separately stating the amount paid to the supplier for that property, the advertising agency is the retailer of the tangible personal property to its client. For example, when the advertising agency invoices a single charge to its client for tangible personal property that includes the amount paid to the supplier for the tangible personal property together with a markup, the advertising agency is the retailer of that tangible personal property and tax applies to that separately stated charge. If the advertising agency makes a lump sum charge to its client that includes the charge for the tangible personal property as well as the charge for any nontaxable services or reproduction rights under	(c)(2) [same as staff's]	(c)(2) [same as staff's]	(c)(2) [same as staff's]	(c)(2) [no comments received]	(b)(2) —(C) Invoice to Client for More Than Cost of Tangible Personal Property to Advertising Agency. When an advertising agency invoices its client for tangible personal property provided by the advertising agency without separately stating the amount paid to the supplier for that property, the advertising agency is the retailer of the tangible personal property to its client. For example, when the advertising agency invoices a single charge to its client for tangible personal property that includes the amount paid to the supplier for the tangible personal property together with a markup, the advertising agency is the retailer of that tangible personal property and tax applies to that separately stated charge. If the advertising agency makes a lump sum charge to its client that includes the charge for the tangible personal property as well as the charge for any nontaxable services or reproduction rights under

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	<p>subdivision (b), the advertising agency is the retailer of the tangible personal property provided and the measure of tax on the sale of that tangible personal property is calculated as provided in subdivision (b).</p> <p><i>[Interested parties have indicated concurrence with staff's proposed language for subdivision (d)– see Exhibit 5, page 10.</i></p> <p>(e) CHARGES AND TRANSACTIONS GOVERNED BY OTHER REGULATIONS.</p> <p><i>[Interested parties have indicated concurrence with staff's proposed language for subdivisions (e)(1), (e)(2), and (e)(4) – see Exhibit 5, page 10.</i></p>					<p>subdivision (b), the advertising agency is the retailer of the tangible personal property provided and the measure of tax on the sale of that tangible personal property is calculated as provided in subdivision (b).</p> <p>(e) CHARGES AND TRANSACTIONS GOVERNED BY OTHER REGULATIONS.</p>
ACTION 3 – New Clarifying Language (Printed Sales Messages)	(3) PRINTED SALES MESSAGES. Qualifying sales of printed sales messages may qualify for exemption, as explained in Regulation 1541.5.	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[same as staff's]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>

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ACTION 21 – General Language Differences	(5) VIDEO OR FILM PRODUCTIONS. When a video or film production obtained or furnished by an advertising agency to its client constitutes qualified production services as defined in Regulation 1529, tax applies to the charges for such qualified production services as provided in Regulation 1529.	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	(4) VIDEO OR FILM PRODUCTIONS. When a video or film production obtained or furnished by an advertising agency to its client constitutes qualified production services as defined in Regulation 1529, tax does not apply applies to the charges for such qualified production services as provided in Regulation 1529. Similarly, tax does not apply to charges for creative art services or for qualified production services.

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*Action Items are not in strict numerical order on this schedule, since some Action Items reference numerous areas of the regulation.

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BOARD OF EQUALIZATION
KEY AGENCY ISSUE

- ☐ Board Meeting
- ☒ Business Taxes Committee
- ☐ Customer Services and Administrative Efficiency Committee
- ☐ Legislative Committee
- ☐ Property Tax Committee
- ☐ Other

Proposed Regulatory Changes Regarding Application of Tax to Graphic Arts and Related Enterprises (Regulations 1540, 1541, 1543 and 1528)

I. Issue

Should Regulations 1540, 1541, 1543 and 1528 be amended to clarify the application of tax to graphic arts and related enterprises?

II. Staff Recommendation

Staff recommends the adoption of amendments to Regulations 1540, 1541, 1543, and 1528 as provided in Exhibits 5, 7, 8, and 9. Staff's recommendations have no operative date. (See Issue Paper (IP) pages 4 through 11.)

III. Other Alternative(s) Considered

A. Alternative 1 - (Agenda D Action Items 14, 16 and 21)

In addition to staff's recommendation, Mr. Eric Miethke representing the Graphic Artists Guild (Guild), proposes amendments to Regulation 1540 as provided in Exhibit 3. The Guild's proposal recommends no operative date. (See IP pages 11 through 13.)

B. Alternative 2 - (Agenda D Action Items 15 and 16)

In addition to staff's recommendation, Mr. Nicholas Blonder, Attorney at Law, proposes amendments to Regulation 1540 as provided in Exhibit 3. Mr. Blonder's proposal recommends no operative date. (See IP pages 13 through 15.)

C. Alternative 3 - (Agenda D Action Items 5-9, 12, and 21)

In addition to staff's recommendation, Mr. Don Wayne proposes amendments to Regulation 1540 as provided in Exhibit 3. Mr. Wayne's proposal recommends no operative date. (See IP pages 15 through 17.)

D. Alternative 4 - (Agenda D Action Items 13 and 17)

In addition to staff's recommendation, Mr. Peter Liao proposes amendments to Regulation 1540 as provided in Exhibit 3. Mr. Liao's proposal recommends no operative date. (See IP pages 17 through 19.)

E. Alternative 5 - (Agenda D Action Items 2, 5-8, 10, 11, and 18-21)

Mr. Don Jung and Mr. Joseph Vinatieri, representing the American Association of Advertising Agencies (AAAA), propose amendments to Regulation 1540 as provided in Exhibits 3 and 4. The AAAA's proposal recommends no operative date. (See IP pages 19 through 20.)

F. Alternative 6 - (Agenda C Action Item 1)

As proposed by Mr. Patrick Leone, CPA, adopt staff's recommendation except do not replace the language "ultimately subject to sales tax" in Regulation 1541(c)(1) as provided in Exhibit 6. If staff's recommendation is approved, Mr. Leone recommends an operative date of October 1, 2002. (See IP pages 20 through 22.)

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IV. Background

The application of tax to graphic arts and related enterprises is addressed in Regulation 1540, *Advertising Agencies, Commercial Artists and Designers*; Regulation 1541, *Printing and Related Arts*; and Regulation 1543, *Publishers*. Please see Exhibit 10 for a summary of the current provisions and history of these three regulations. Clarification of the application of tax is needed for the following reasons:

- Amendments to Regulations 1540 and 1541, effective 1999 and 2000, have resulted in inconsistencies and confusion in the application of tax to charges for graphic art services and special printing aids.
- The April 2, 2001 California Supreme Court decision, *Preston v. State Board of Equalization* invalidated a portion of Regulation 1540.
- Regulation 1543 has not been updated to correspond with the 1999 and 2000 amendments to Regulations 1540 and 1541.
- Senate Bill (SB) 330, Chapter 799, Statutes of 1999, created Revenue and Taxation Code (RTC) section 6010.30 that provides an exclusion from “sale” or “purchase” for certain transfers of original drawings, sketches, illustrations, or paintings by artists or designers at a social gathering. These provisions are not currently in Regulation 1540.
- In order to alert commercial photographers who are acting as commercial artists that the application of tax to their transactions is explained in Regulation 1540, a reference to Regulation 1540 should be added to Regulation 1528, *Photographers, Photo Copiers, photofinishers and X-Ray Laboratories*.

Application of Tax to Charges for Special Printing Aids

The provision including the phrase “ultimately subject to sales tax” in Regulation 1541(c)(1) has created confusion. This is evident by taxpayers’ written requests for clarification on the terminology “ultimately subject to sales tax” because it referred to transactions involving exempt sales as well as taxable sales.

Provisions in Regulation 1543 concern the application of tax to sales of artwork to publishers. These provisions use language taken from Regulation 1540 prior to the amendments that became effective on April 23, 2000. Consequently, Regulation 1543 does not address the situation where there is a taxable sale of artwork along with nontaxable conceptual and design services for a lump-sum price, thereby creating a potential inconsistency between Regulations 1540 and 1543.

Preston Decision

On April 2, 2001, the California Supreme Court issued its opinion in the case of *Preston v. State Board of Equalization* (2001) 25 Cal.4th 197 (*Preston*). *Preston* found that tax does not apply to a copyright interest transferred along with copyrighted artwork pursuant to a written agreement contemplating the copying and selling of the copyrighted material because this type of transaction constitutes a technology transfer agreement (TTA) pursuant to RTC sections 6011(c)(10) and 6012(c)(10). In reaching this conclusion, *Preston* further found that the legislation enacting the TTA provisions applied retroactively and that at least subdivision (d)(4) of Regulation 1540 is invalid.

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Since the *Preston* decision specifically invalidated a subdivision of Regulation 1540 and provides a method of valuing artwork that differs from the current provisions of 1540, it is proposed that Regulation 1540 be amended in accordance with the *Preston* decision.

As a separate but related matter, proposed Regulation 1507, *Technology Transfer Agreements*, was discussed at the December 19, 2001 Business Taxes Committee meeting, and is scheduled for public hearing on March 27, 2002.

Senate Bill 330

Senate Bill (SB) 330 (Chapter 799, Statutes 1999) created RTC section 6010.30, which provides an exclusion from the terms “sale” and “purchase” for the transfer of original drawings, sketches, illustrations or paintings by an artist or designer at a social gathering for entertainment purposes if all of the following requirements are met:

- Substantially all (80 percent or more) of the drawings, sketches, illustrations, or paintings are delivered by the artist or designer to a person or persons other than the purchaser.
- Substantially all (80 percent or more) of the drawings, sketches, illustrations, or paintings are received by a person or persons, other than the purchaser, at no cost to the person or persons who become the owner of the drawings or sketches.
- The charge for the drawings, sketches, illustrations, or paintings is based on a preset fee.
- The fee charged for the drawings, sketches, illustrations, or paintings is contingent upon a minimum number of three drawings, sketches, illustrations or paintings to be produced by the artist or designer at the social gathering.

This legislation was enacted to codify a specific ruling in a case heard by the Board. That case involved an artist who was hired for an hourly fee by a host or hostess to draw caricatures of guests at parties. The artist received the fee regardless of the number of guests who requested that a caricature be drawn. The Board concluded that the entertainment value the artist provided was the true object of the contract and that any artwork transferred was merely incidental. It is proposed that the provisions of RTC section 6010.30 be incorporated into Regulation 1540.

Submissions From Interested Parties

Staff has received comments from the Printing Industries of California (PIC), the Graphic Artists Guild (Guild), the American Association of Advertising Agencies (AAAA), Sedlik Photography, the American Society of Media Photographers (ASMP), and the California chapters of the Advertising Photographers of America (APA). See below for further discussion of submissions received.

Interested parties meetings were held on August 7, 2001, and on November 13, 2001, in both Sacramento and Torrance via teleconference to discuss the concerns of the graphic arts industries.

Subsequent to the November 13, 2001 interested parties meeting, staff received additional comments from AAAA, Guild, PIC, Mr. Peter Liao, Mr. Nicholas Blonder, and Mr. Don Wayne.

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In addition to comments from interested parties, staff has considered input from the field audit staff and other subject matter experts within the Board when drafting the proposed amendments. This was done in an effort to encompass situations encountered in the field throughout California.

This topic is scheduled for discussion at the February 5, 2002 Business Taxes Committee meeting.

V. Staff Recommendation

A. Description of the Staff Recommendation

Staff recommends the following:

- Conforming Regulations 1540, 1541, and 1543 in accordance with the April 2000 revisions to Regulation 1540, in regard to lump-sum billings for artwork and nontaxable services. Staff's proposal clarifies that printers and publishers are entitled to claim 75% of a lump-sum charge for the transfer of artwork as nontaxable charges if conceptual and design services are provided with the artwork.
- Amending Regulation 1540 in accordance with the California Supreme Court ruling in *Preston v. State Board of Equalization* on the taxability of artwork when sold along with copyright interests. Staff proposes to insert language and references on the application of tax to technology transfer agreements in Regulations 1540, 1541, and 1543. In addition, staff proposes language to clarify when transfers of copyright interests are includable in the taxable sales price and when transfers of copyright interests along with copyrighted artwork, pursuant to a written agreement contemplating the copying and selling of the copyrighted material, are not taxable.
- Reformatting Regulation 1540 to provide definitions of terms and the application of tax at the beginning of the regulation. Staff proposes to define key terms for each regulation to provide an easier understanding of the application of tax to graphic arts and related enterprises.
- Amending Regulation 1540 to clarify that the term "commercial artists" includes commercial photographers. As part of incorporating commercial photographers in Regulation 1540, the term "photographs" was replaced with "photographic images" to include tangible personal property provided by commercial photographers and designers. Staff proposes to incorporate language in subdivision (a)(3) to include a commercial photographer within the same classification as a commercial artist.
- Adding the following sentence to Regulation 1528, *Photographers, Photocopiers, Photo Finishers and X-ray Laboratories*, to refer commercial photographers to Regulation 1540.

See Regulation 1540, *Advertising Agency and Commercial Artists*, for transfers of photographic images by commercial artists.

- Incorporating into Regulation 1540(d) the provisions of SB 330, which specifies the circumstances under which tax does not apply to the transfer of original drawings at social gatherings for entertainment purposes.

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- Amending Regulation 1541 to replace the confusing terminology of “ultimately subject to tax” with a clear explanation of the application of tax. Staff proposes to reformat the discussion of special printing aids into subdivision (c)(1) through (c)(3) as it relates to a printer’s and a print broker’s purchase of special printing aids, the sale of these printing aids, and the application of tax to each transaction.

Staff’s recommendations have no operative date. Staff’s proposed language is shown in Exhibits 5, 7, 8, and 9.

Mr. Gerald M. Bonetto representing the Printing Industries of California (PIC), has provided comments addressing the inconsistency between Regulations 1540 and 1541. Staff has worked with PIC and has addressed their concerns with regard to the printing industry. The PIC has provided their support and agreement with staff’s recommendation in regard to the proposed amendments to Regulation 1541.

Several interested parties have expressed agreement with staff’s intentions, except as explained in the following discussion of alternative proposals. Proposals 1 through 5 relate to Regulation 1540, and subdivision references in these proposals are to Regulation 1540. Proposal 6 relates to Regulation 1541.

Staff’s Comments Regarding Guild’s Proposal (Alternative 1)

As described under Alternative 1, the Guild proposes to provide language in subdivision (b)(2)(D)2. to provide that finished artwork temporarily transferred on computer storage media in a technology transfer agreement has a de minimis fair rental value and that the value of the artwork is incidental to the transfer of the intangible rights. Staff believes that this proposal does not conform with law and does not agree with it. Although the Guild refers to Regulation 1502 (discussed further below), staff believes that the circumstances here are different. RTC sections 6011(c)(10) and 6012(c)(10) explicitly set forth the measure of tax on the sale of tangible personal property in connection with a technology transfer agreement, and do not incorporate a de minimis concept. In fact, these provisions explicitly apply this measure of tax to temporary transfers (i.e., leases). Thus, in accordance with these provisions, staff believes that there is no statutory authority to allow a de minimis concept in the valuation of the tangible personal property transferred in a technology transfer agreement, and that tax must instead be applied as specified in the provisions of the Revenue and Taxation Code.

Furthermore, the Guild’s argument is the same argument it made as *Amicus Curiae* before the California Supreme Court in *Preston*. The Court explicitly rejected this argument and held that these types of transfers are not merely incidental to the transfer of a copyright, but instead are “taxable transfers of tangible property.” (*Preston v. State Board of Equalization* (2001) 25 Cal.4th 197, 208.) The Court specifically recognized the obvious: the transfer involves the taxable transfer of the tangible personal property plus the transfer of the copyright interest which is not taxable under the technology transfer provisions of RTC sections 6011(c)(10) and 6012(c)(10). The Court then proceeded to address the very question raised here, that is, how tax applies to a temporary transfer of tangible personal property as part of a technology transfer agreement. The Court held that since the agreements did not separately state a price for the tangible personal property, that “the amount subject to taxation is either ‘the price at which the tangible personal property was sold, leased, or offered to third parties’ (§§ 6011(c)(10)(B), 6012(c)(10)(B)), or ‘200 percent of the cost of materials and labor used to produce the tangible personal property subject to tax’ (§§ 6011(c)(10)(C), 6012(c)(10)(C)).” (*Id.* 25 Cal.4th 225.) The regulation should not conflict with the guidelines set forth by the California Supreme Court. The regulation as proposed by staff accomplishes the purpose of the statute and is consistent with the *Preston* decision.

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The Guild proposes to provide language in subdivision (b)(2)(D)2.a. that the measure of tax on a transfer of finished art in a technology transfer agreement is a “reasonable” value. Staff believes that the term “fair market value” is a proper interpretation of what constitutes “reasonable” for these purposes. Accordingly, staff recommends conforming the changes in Regulation 1540 to proposed Regulation 1507.

The Guild proposes in subdivision (b)(2)(D)(2)c. to clarify that “labor cost” used to produce tangible personal property includes only charges for labor that are paid to a third party or performed by an employee of the advertising agency or commercial artist. Staff agrees that amounts paid to third parties are a basis for determining labor costs for the valuation of tangible personal property transferred in conjunction with an intangible copyright interest. However, staff does not agree that the labor of an individual artist has no value or that there is no cost to the artist when he or she works on a particular project rather than doing something else. For example, the longer an artist takes to produce a piece of art, the greater the cost of the artist’s labor and, presumably, the greater the sale price to the purchaser.

In standard economic models, the costs of doing business include not only those payments to third parties for labor, materials, and other expenses, but also implied costs and opportunity costs. The implied cost of the owner’s own labor equals the return on that labor. One method of valuing that labor is to simply value the property created with that labor (less costs of materials). Another method for valuing the owner’s labor is to use the opportunity cost of that labor, which can be measured by the cost of forgoing the wages from a salaried position in favor of pursuing self-employment. The value of artwork created by an artist is certainly not less when the artist uses his or her own labor to produce the art rather than paying a third party for the labor to produce the art. Since the cost of labor is necessarily (and statutorily) a component of the value of that art, the value of the artist’s own labor in producing the artwork cannot be regarded as less valuable than the labor of a third party (and certainly cannot be regarded as having no value). Thus, in summary, staff believes that the value of the labor should be the same whether provided by the artist or by a third party.

If staff’s recommendation is adopted, the Guild proposes a rebuttable presumption that the fair market value for the artist’s self-consumed labor for preparation of the finished art shall be presumed to be \$100 in the absence of evidence of a price charged by the commercial artist or advertising agency for labor only. Staff believes that the fair market value of the artists time will vary significantly from job to job and that a presumption of \$100 would not be representative for these type of transactions.

Staff’s Comments Regarding Mr. Nicholas Blonder’s Proposal (Alternative 2)

Mr. Nicholas Blonder proposes to add language to subdivision (b)(2)(D)2.a. referencing separately stated rent for the temporary possession of finished art, in addition to staff’s proposed language regarding the separately stated sales price for the finished art. Staff agrees that the language “stated sales price” applies to a lease as a continuing sale, and thus staff believes that the added language is not necessary. Further, staff believes that the language “fair market value” includes the fair market value for leases. Therefore, no additional language is recommended by staff.

Mr. Blonder proposes that in subdivision (b)(2)(D)2.c., the “cost of labor” include only consideration paid to an employee or an independent contractor for labor used to create the tangible personal property. Staff’s arguments are the same as for the Guild’s proposal concerning labor.

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Staff's Comments Regarding Mr. Don Wayne's Proposal (Alternative 3)

Mr. Wayne proposes language in Regulation 1540 to clarify that finished art is used to produce special printing aids and that intermediate production aids are used to produce finished art. In addition, Mr. Wayne believes that the definition of preliminary art should provide an implication that the same business entity that prepared the preliminary art, subsequently prepares the finish art on the client's approval of the preliminary art. Staff does not agree with either proposal since staff believes that the proposed changes to the definitions would render them incorrect. With respect to intermediate production aids and special printing aids, staff believes that finished art is used to prepare intermediates, which are then used to prepare special printing aids. With respect to preliminary art, staff believes that the proposed changes could be misread to mean that charges for preliminary art are taxable if no final art is ever delivered. Staff believes the wording of the regulation pertaining to preliminary art is correct and complete as drafted.

Mr. Wayne proposes language be added to subdivision (b)(1)(A)2. to clarify that a title clause in a contract of sale can pass title to tangible personal property to the client prior to use when tangible personal property is developed and used during services performed to convey ideas. Staff believes that including such language could be misleading, and therefore recommends against including this language in the regulation.

Mr. Wayne proposes to amend subdivision (b)(1)(F) to categorize specific nontaxable charges as "markup" and include language on nontaxable agent fees and to amend subdivision (b)(2)(C) to provide clarifying language that there is an option to separately state intermediate production aids as a retail sale or as an agent transaction. Staff believes the discussion of the application of tax to agency fees belongs in the part of the regulation that pertains to such activities. Such agency fees arise only when an advertising agency acts as an agent of its client for the purchase of tangible personal property, and this topic is specifically covered in subdivision (c)(1). Subdivision (c)(1)(B) explicitly states that tax does not apply to a separately stated agency fee when the advertising agency acts as the agent of its client for the purchase of tangible personal property. Accordingly, staff believes that its proposed language in subdivision (c)(1)(B) fully addresses the application of tax to charges for services provided by advertising agencies when they act as the agents of their clients. Subdivision (b)(1)(F), on the other hand, lists nontaxable services which are unrelated to the sale of tangible personal property. It explains that such charges are not taxable when separately stated, and even if not separately stated, they are not part of "direct labor" for purposes of subdivision (b)(3) when the charge for these services are combined with charges by the advertising agency or commercial artist for its sale of tangible personal property. A fee for acting as an agent for the purchase of tangible personal property would never come within this provision because it would never be a nontaxable agency fee if related to a sale of tangible personal property *by the advertising agency or commercial artist*. Staff thus believes that the added language is not appropriate for subdivision (b)(1)(F). Furthermore, the proposed terminology is incorrect in that the term "markup" normally connotes a taxable component. Staff also believes that the clarifying language proposed for subdivision (b)(2)(C) in regard to retail sales and agent transactions is not appropriate in the subdivision referenced by Mr. Wayne, since the subject to this paragraph is addressing combined charges of finished art that are combined with charges for conceptual design services.

Mr. Wayne believes that clarification on the definition of "incorporated" is necessary for taxpayers to fully understand which materials can be purchased for resale in subdivision (c)(2)(B). In addition, Mr. Wayne proposes to provide examples to clarify when the materials are incorporated into finished art

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and when they are not. Staff believes that the language is clear on what “incorporated” means and that the examples Mr. Wayne suggests are more appropriate for inclusion in Pamphlet No. 37, *Tax Tips for The Graphic Arts Industry*, or Pamphlet No. 38, *Tax Tips for Advertising Agencies*. Staff believes that the additional language is unnecessary in the regulation, but will consider adding the proposed examples to the referenced pamphlets.

Staff’s Comments Regarding Mr. Peter Liao’s Proposal (Alternative 4)

Mr. Liao proposes language to clarify the application of tax in regard to reproduction rights transferred with finished art. First, Mr. Liao believes that neither the statute nor the *Preston* case requires a technology transfer agreement to be in writing. Second, Mr. Liao believes that the cost of materials should only be those that are physically incorporated into the tangible personal property.

Staff addressed the issue of the written agreement requirement in proposed Regulation 1507, *Technology Transfer Agreements*. The California Supreme Court has explicitly held that under federal law, an assignment or license of a copyright requires a writing. (*Preston, supra*, 25 Cal.4th 214.) In fact, the Supreme Court also noted that under California State law as well, absent an express written agreement, the transfer of tangible artwork does not transfer the right of reproduction. (*Id.* at 220.) Thus, only a written agreement assigning or licensing the copyright would be effective to transfer such rights, which means that only a written agreement could qualify as a technology transfer agreement under RTC sections 6011(c)(10) and 6012(c)(10). Omitting this requirement from the regulation would be misleading since the Board must in any event follow the ruling of the Supreme Court. Staff recommends that Regulation 1540 be consistent with proposed Regulation 1507.

In addition, staff disagrees that the “cost of materials” is only the cost of materials incorporated into the finished art. Staff believes that the cost of materials used to produce the finished art includes the cost of materials consumed as part of the production of the finished art as well as the cost of the materials physically incorporated into that finished art.

Staff’s Comments Regarding AAAA’s Proposal (Alternative 5)

After analyzing the AAAA’s proposed language, it appears that AAAA is combining the old format and the new format as recommended by staff, in addition to providing new interpretations of:

- Clip-art. AAAA proposes that clip-art be considered an intermediate production aid. Staff believes that clip-art qualifies as typography and is not an intermediate production aid which is taxable. AAAA’s interpretation would reverse the existing interpretation so that transfers currently regarded as nontaxable typography would become taxable. (Exhibit 4, subdivision (a)(8).)
- Preliminary art. AAAA proposes that preliminary art be regarded as incidental to the true object of the transaction. However, when the contract provides for delivery of final art, regarding preliminary art as incidental to the true object of the contract would mean that it is incidental to the sale of finished art, which in turn would mean that the charge for the preliminary art is taxable as part of the sale of the finished art. Staff does not agree that preliminary art should be regarded as incidental to the selling of finished art when the parties satisfy the current rules for regarding the preliminary art stage as separate from the finished art stage. Staff also disagrees to the extent that AAAA’s proposal seeks to permit the parties to contract for the actual sale of the tangible personal property comprising the finished art (i.e., providing in the contract that the client will obtain title to or permanent

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possession of such tangible personal property) and then disregard the agreement for that sale and regard the contract as a service. The proposal is ambiguous in that it is susceptible to either of these disparate interpretations. In either event, the interpretation would be a substantial change from current law, providing either that: 1) charges for preliminary art are taxable under circumstances where they are nontaxable under the current regulation and under staff's proposal; or 2) that charges for preliminary art are not taxable even when the parties agree that the charges are for the sale of tangible personal property (i.e., for the transfer of title to the preliminary art), again contrary to the current regulation and staff's proposal. (Exhibit 4, subdivision (a)(10).)

AAAA proposes language that they believe provides a more "user friendly" regulation without undue complexity. They have incorporated some of staff's recommended changes and have provided alternative language. AAAA believes that staff's new version is more complex than the previous draft and are of the opinion that the existing regulation is quite satisfactory to the industry.

Staff incorporated a few of AAAA's suggestions with some modified language that staff believes addresses part of their concerns. However, staff believes that its language is clearer and that its suggested new format is consistent with other regulations, which make the proposed regulation easier to understand and follow. Other interested parties agree with staff that the new format is preferable to the old format.

Staff's Comments Regarding Mr. Patrick Leone's Proposal (Alternative 6)

Mr. Patrick Leone, CPA, proposes that the terminology "ultimately subject to sales tax" as used in Regulation 1541 not be replaced. In addition, if the phrase is deleted, Mr. Leone proposes that the change be applied on a prospective basis. Mr. Leone believes that this language clearly exempts resales, which are ultimately sold and taxed. Staff believes that replacing the terminology "ultimately subject to tax" does not change the application of tax or the meaning of the regulation. The amendments proposed by staff in subdivision (c) retain the tax application of the current language but in a manner that clearly describes the application of tax to each transaction whether it is a retail sale of printed matter and special printing aids or a nontaxable sale of printed matter and special printing aids. In addition, the terminology "ultimately subject to sales tax" is technically incorrect in that it refers to transactions which are not, in fact, subject to sales tax. Staff believes that the Board's own sales and use tax regulations should not use terminology that is incorrect on its face. This incorrect use of the terminology is part of the reason that this portion of the regulation has caused confusion within the industry and among audit staff.

Staff also notes that Mr. Gerald Bonetto of the Printing Industries of California has expressed his support for staff's proposed amendments to Regulation 1541.

B. Pros of the Staff Recommendation

- Provides conformity among Regulations 1540, 1541, and 1543 with the April 2000 revisions to Regulation 1540.
- Considers commercial photographers as commercial artists.
- Provides consistency in formatting of the regulations.

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- Provides clarity on the application of tax to the graphic arts industry.
- Organizes Regulation 1540 in a more logical and easy to read manner.
- Incorporates the ruling in the *Preston* decision in regard to technology transfer agreements.
- Incorporates the provisions of SB 330.

C. Cons of the Staff Recommendation

Requires regulatory change.

D. Statutory or Regulatory Change

No statutory change required. However, staff's recommendation does require amendments to Regulations 1540, 1541, 1543, and 1528.

E. Administrative Impact

Staff will be required to notify taxpayers of the amendments to the regulations through an article in the Tax Information Bulletin. In addition, revisions to various procedures manuals and Board publications may be needed.

F. Fiscal Impact

1. Cost Impact

No additional cost. Staff will notify taxpayers of the regulation amendments through a Tax Information Bulletin (TIB) article. The workload associated with publishing and distributing the TIB is considered routine and any corresponding cost would be within the Board's existing budget. Similarly, the workload associated with revising procedure manuals and Board publications is considered routine and any corresponding cost would be within the Board's existing budget.

2. Revenue Impact

None. See Revenue Estimate (Exhibit 1).

G. Taxpayer/Customer Impact

- Customers will have the same tax treatment for the same services provided by printers, commercial artists, or advertising agencies.
- Confusion within the graphic arts industry regarding the application of tax will be reduced.

H. Critical Time Frames

The proposed amendments represent interpretations of existing statutes, and therefore have no operative date. Implementation will take place 30 days following approval of the regulations by the Office of Administrative Law.

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VI. Alternative 1

A. Description of the Alternative

As proposed by Mr. Eric Miethke representing the Graphic Artists Guild (Guild), adopt staff's recommendation except amend Regulation 1540 to:

- Provide language in subdivision (b)(2)(D)2 to clarify that finished artwork temporarily transferred on computer storage media in a technology transfer agreement has a de minimis fair rental value and the value of the artwork is incidental to the transfer of the intangible rights.
- Provide language in subdivision (b)(2)(D)2.a. to clarify that the measure of tax on a transfer of finished art in a technology transfer agreement is a "reasonable" value and not a "fair market value."
- Provide language in subdivision (b)(2)(D)(2)c. to clarify that "labor cost" used to produce tangible personal property includes only charges for labor that are paid to a third party or performed by an employee of the advertising agency or commercial artist. If staff's recommendation is adopted, the fair market value for the artist's self-consumed labor for preparation of the finished art shall be presumed to be \$100 in the absence of evidence of a price charged by the commercial artist or advertising agency for labor only.

Temporary Transfers of Finished Art

The Guild acknowledges that when the transfer of tangible personal property in a technology transfer agreement is a temporary transfer, the measure of tax is the fair rental value of the property. The Guild believes that in the commercial art context, temporary transfers of finished art may be as simple as handing over a computer diskette with electronically stored finished art on it to a client who then copies the file to their own computer and returns the diskette to the artist. The Guild believes that the fair rental value of such finished art is de minimis and not worth staff's time to determine the measure of tax on these transactions. The Guild believes that the Board has used this interpretation in similar contexts without explicit statutory authority (Regulation 1502(f)(1)(B), "any storage media used to transmit the program is merely incidental").

Reasonable Value for Finished Art

The Guild disagrees with staff's recommendation that the separately stated charge for finished art in a technology transfer agreement has to be a "fair market value" when the statute specifies a "reasonable" value. According to the Guild, staff has used this language in other regulations and believes that it should also be used in Regulation 1540.

Cost of Labor Used to Produce Finished Art

The Guild believes that "cost" has meaning in the context of labor "purchased" by the artist from a third party who is either an employee (in the form of wages) or an independent contractor, because the statute is looking for an objectively measurable labor component to gross up to arrive at a price for the tangible personal property. The Guild believes that staff's interpretation of the labor costs

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used to produce finished art exceeds the scope of section 6011(c)(10) and 6012(c)(11) because those statutes speak in term of “costs” and in this case the transferor of the intangible rights to reproduce and the tangible personal property at issue will have no “costs” if they perform the work themselves and do not hire third parties to produce to finished art. For that reason, if the preparation of the finished art is by the artist himself or herself, it has no “cost” to the artist, and therefore, such self-consumed labor performed by the artists themselves should be excluded from the “cost” of labor. As an alternative, if staff’s recommendation is adopted, the Guild proposes a rebuttable presumption, in the absence of an objectively verifiable “cost” of labor paid to a third party, that the labor component of finished art transferred on an electronic file is not more than \$100.

The Guild’s proposal has no operative date, and is shown in Exhibit 3.

B. Pros of the Alternative

- Allows finished art temporarily transferred on computer storage media in technology transfer agreements to be considered de minimis thereby avoiding the application of any tax to the transfer. The commercial artist would be a consumer of the computer storage media.
- Minimizes the application of tax to the transfer by interpreting labor “costs” in technology transfer agreements to include only labor purchased from third parties or employees. This would result in a lower labor valuation by excluding any self-consumed labor performed by the commercial artists themselves.

C. Cons of the Alternative

- Requires regulatory change.
- Ignores the statutory directives of the Revenue and Taxation Code and the guidelines set forth in the *Preston* decision.
- Provides less guidance (possibly leading to more disputes) by using the less specific term “reasonable” rather than “fair market value.”

D. Statutory or Regulatory Change

No statutory change required. However, this alternative does require amendments to Regulation 1540.

E. Administrative Impact

Staff will be required to notify taxpayers of the amendments to the regulation through an article in the Tax Information Bulletin. In addition, revisions to various procedures manuals and Board publications may be needed.

F. Fiscal Impact

1. Cost Impact

No additional cost. Staff will notify taxpayers of the regulation amendments through a Tax Information Bulletin (TIB) article. The workload associated with publishing and distributing the TIB is considered routine and any corresponding cost would be within the Board’s existing budget. Similarly, the workload associated with revising procedure manuals and

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Board publications is considered routine and any corresponding cost would be within the Board's existing budget.

2. Revenue Impact

See Revenue Estimate (Exhibit 1).

G. Taxpayer/Customer Impact

Permits individual taxpayers who produce tangible personal property, pursuant to a technology transfer agreement that provides finished art with reproduction rights, to exclude their own labor from the calculation of "costs" of labor.

H. Critical Time Frames

The proposed amendments represent interpretations of existing statutes, and therefore have no operative date. Implementation will take place 30 days following approval of the regulation by the Office of Administrative Law.

VII. Alternative 2

A. Description of the Alternative

As proposed by Mr. Nicholas Blonder, Attorney at Law, adopt staff's recommendation except:

- Add language to proposed Regulation 1540(b)(2)(D)2.a. referencing separately stated rent for the temporary possession of finished art, in addition to staff's proposed language regarding the separately stated sales price for the finished art; and
- Amend Regulation 1540(b)(2)(D)2.c., when there is no such separately stated sales price for the finished art, to include in the "cost of labor" only consideration paid to an employee or an independent contractor for labor used to create such tangible personal property.

Fair Rental Value for Temporary Transfers of Finished Art

According to Mr. Blonder, since the court characterized the transfers of Preston's artwork as "leases," a reproduction rights license agreement should also be able to establish fair rental value as a reasonable "price" for a temporary transfer of tangible artwork. Under this circumstance, there is no "sales price" in the commonly understood sense. Blonder believes that the added language makes clear that, in the case of a *temporary* transfer of artwork, the agreement may stipulate a fair *rental* value. Accordingly, this would be consistent with the Supreme Court's conclusion that the transfers of Ms. Preston's artwork fell within the definition of a lease.

Definition of Labor Costs

According to Mr. Blonder, an artist who works alone and does not use the services of employees, has no labor costs since the dictionary definition of "cost" is clearly based on the transfer of consideration from one person or entity to another. *The Random House Dictionary of the English*

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Language (Random House, 1969) defines “Cost” as “the price paid to acquire, produce, accomplish, or maintain anything.” The *American Heritage Dictionary of the English Language* (Houghton Mifflin, 1976) defines cost as “An amount paid or required in payment for a purchase.” Mr. Blonder believes that an artist’s personal efforts may be considered “labor,” but he or she does not pay a “cost” for such labor.

In addition, Mr. Blonder believes that the Board has no power to impute the measure of tax from circumstances other than cost in subdivision (b)(2)(D)2.c.. According to Mr. Blonder, staff’s proposed language creates a valuation standard that imputes a labor cost and that only the Legislature has constitutional authority to amend the technology transfer agreement statutes. Mr. Blonder believes that his proposed language deletions eliminate the unauthorized imputation of a “cost” of labor. The added language provides examples of objectively ascertainable labor costs which properly fall within the scope of the technology transfer agreement statutes.

Mr. Blonder’s proposal has no operative date and is shown in Exhibit 3.

B. Pros of the Alternative

- Provides clarification that leases of temporary transfers of artwork in technology transfer agreements is valued at the fair rental value for purposes of computing the measure of tax.
- Minimizes the application of tax to the transfer by interpreting labor “costs” in technology transfer agreements to include only labor purchased from third parties or employees. This would result in a lower labor valuation by excluding any self-consumed labor performed by the commercial artists themselves.

C. Cons of the Alternative

- Requires regulatory change.
- Ignores the statutory directives of the Revenue and Taxation Code and the guidelines set forth in the *Preston* decision.
- Adds confusing and unnecessary language to the regulation.

D. Statutory or Regulatory Change

No statutory change required. However, this alternative does require amendments to Regulation 1540.

E. Administrative Impact

Staff will be required to notify taxpayers of the amendments to the regulation through an article in the Tax Information Bulletin. In addition, revisions to various procedures manuals and Board publications may be needed.

F. Fiscal Impact

1. Cost Impact

No additional cost. Staff will notify taxpayers of the regulation amendments through a Tax Information Bulletin (TIB) article. The workload associated with publishing and distributing

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the TIB is considered routine and any corresponding cost would be within the Board's existing budget. Similarly, the workload associated with revising procedure manuals and Board publications is considered routine and any corresponding cost would be within the Board's existing budget.

2. Revenue Impact

See Revenue Estimate (Exhibit 1).

G. Taxpayer/Customer Impact

Permits individual taxpayers who produce tangible personal property, pursuant to a technology transfer agreement that provides finished art with reproduction rights, to exclude their own labor from the calculation of "costs" of labor.

H. Critical Time Frames

The proposed amendments represent interpretations of existing statutes, and therefore have no operative date. Implementation will take place 30 days following approval of the regulation by the Office of Administrative Law.

VIII. Alternative 3

A. Description of the Alternative

As proposed by Mr. Don Wayne, adopt staff's recommendation except amend Regulation 1540 to:

- Amend the definitions for subdivisions (a)(6) on finished art, (a)(8) on intermediate production aids, and (a)(10) on preliminary art.
- Amend subdivision (b)(1)(A)1. to incorporate the concept of a nontaxable "killed job" in reference to preliminary art and final art.
- Amend subdivision (b)(1)(A)2. to provide language that a title clause in a contract can pass title to artwork prior to use.
- Amend subdivision (b)(1)(F) to categorize specific nontaxable charges as "markup" and include language on nontaxable agent fees.
- Amend subdivision (b)(2)(C) to provide clarifying language that there is an option to separately state intermediate production aids as a retail sale or as an agent transaction.
- Amend subdivision (c)(2)(B) to further define the term "incorporated" and provide examples.

Definition of Terms

Mr. Wayne is proposing language to clarify that finished art is used to produce special printing aids and that intermediate production aids are used to produce finished art. In addition, Mr. Wayne believes that the definition of preliminary art should provide an implication that the same business entity that prepared the preliminary art, subsequently prepares the finish art on the client's approval of the preliminary art. Mr. Wayne believes that the preliminary art exists only if the approved

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preliminary art results in the preparation of finished art. The true intent of preliminary art is to secure approval to proceed with finished art. Therefore, Mr. Wayne believes that the transfer of any tangible personal property as part of this approval phase is incidental to the ideas presented and should not be taxable. If the producing of the preliminary art does not subsequently result in the client's approval, such job is referred to as a "killed job." Mr. Wayne suggests incorporating the concept of a "killed job" because according to Mr. Wayne, the true intent of preliminary art is either to gain client approval to proceed with the preparation of finished art, or to provide nontaxable intangible consulting services.

Title Clause in Contract of Sale

Mr. Wayne proposes regulatory language in subdivision (b)(1)(A)2. to clarify that a title clause in a contract of sale can pass title to tangible personal property to the client prior to use when tangible personal property is developed and used during services performed to convey ideas.

Specific Nontaxable Charges

Mr. Wayne believes that the discussion of specific nontaxable charges should be addressing what is included rather than what is not included. Therefore, Mr. Wayne has provided suggested language for subdivision (b)(1)(F) to clarify that the fees and commissions that are not taxable, are considered to be "markup" for purposes of determining the selling price of retail sales by an advertising agency and commercial artist in subdivision (b)(3). Mr. Wayne is also proposing to add back the language staff deleted from this subdivision in reference to nontaxable agent fees added to the charge for tangible personal property by agencies established as agents for their clients.

In regard to separately stating charges, Mr. Wayne proposes to add language to subdivision (b)(2)(C) to clarify that an advertising agency has an option to separately state intermediate production aids as a retail sale or as an agent transaction as discussed in subdivision (c).

Definition of the Term "Incorporated"

Mr. Wayne believes that clarification on the definition of "incorporated" is necessary for taxpayers to fully understand which materials can be purchased for resale. In addition, Mr. Wayne proposes to provide examples to clarify when the materials are incorporated into finished art and when they are not.

Mr. Wayne's proposal has no operative and is shown in Exhibit 3.

B. Pros of the Alternative

Provides what the proponent regards as additional clarifying language for definitions of terms.

C. Cons of the Alternative

- Requires regulatory change.
- Adds language that is redundant, confusing, or incorrect.
- Adds language which more properly belongs in a Tax Tip Pamphlet.

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D. Statutory or Regulatory Change

No statutory change required. However, this alternative does require amendments to Regulation 1540.

E. Administrative Impact

Staff will be required to notify taxpayers of the amendments to the regulation through an article in the Tax Information Bulletin. In addition, revisions to various procedures manuals and Board publications may be needed.

F. Fiscal Impact

1. Cost Impact

No additional cost. Staff will notify taxpayers of the regulation amendments through a Tax Information Bulletin (TIB) article. The workload associated with publishing and distributing the TIB is considered routine and any corresponding cost would be within the Board's existing budget. Similarly, the workload associated with revising procedure manuals and Board publications is considered routine and any corresponding cost would be within the Board's existing budget.

2. Revenue Impact

See Revenue Estimate (Exhibit 1).

G. Taxpayer/Customer Impact

Taxpayers will receive specific instructions that when acting as retailers, they can add a title clause in their contracts if tangible personal property is to be transferred to the client prior to any use by the advertising agencies or commercial artists. The proposed language, particularly the use of the term "markup" in subdivision (b)(1)(F), could cause confusion in the graphic arts industry.

H. Critical Time Frames

The proposed amendments represent interpretations of existing statutes, and therefore have no operative date. Implementation will take place 30 days following approval of the regulation by the Office of Administrative Law.

IX. Alternative 4

A. Description of the Alternative

As proposed by Mr. Peter Liao, adopt staff's recommendation except amend Regulation 1540 to:

- Provide in subdivision (b)(2)(D)2. that *any* agreement would qualify as a technology transfer agreement.
- Clarify in subdivision (b)(2)(D)2.c. that the "cost of materials" only consists of those materials physically incorporated into the finished art or tangible personal property transferred as part of a technology transfer agreement.

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Mr. Liao's proposal has no operative date and is shown in Exhibit 3.

B. Pros of the Alternative

Provides a more liberal interpretation of technology transfer agreements.

C. Cons of the Alternative

- Requires regulatory change.
- Is contrary to the California Supreme Court's decision in *Preston*.
- Is inconsistent with the Board's decisions regarding technology transfer agreements in proposed Regulation 1507.

D. Statutory or Regulatory Change

No statutory change required. However, this alternative does require amendments to Regulation 1540.

E. Administrative Impact

Staff will be required to notify taxpayers of the amendments to the regulation through an article in the Tax Information Bulletin. In addition, revisions to various procedures manuals and Board publications may be needed.

F. Fiscal Impact

1. Cost Impact

No additional cost. Staff will notify taxpayers of the regulation amendments through a Tax Information Bulletin (TIB) article. The workload associated with publishing and distributing the TIB is considered routine and any corresponding cost would be within the Board's existing budget. Similarly, the workload associated with revising procedure manuals and Board publications is considered routine and any corresponding cost would be within the Board's existing budget.

2. Revenue Impact

See Revenue Estimate (Exhibit 1).

G. Taxpayer/Customer Impact

Allows inconsistent application of tax in regard to technology transfer agreements to the extent the language differs from that of proposed Regulation 1507.

H. Critical Time Frames

The proposed amendments represent interpretations of existing statutes, and therefore have no operative date. Implementation will take place 30 days following approval of the regulation by the Office of Administrative Law.

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X. Alternative 5

A. Description of the Alternative

Mr. Don Jung and Mr. Joseph Vinatieri, representing the American Association of Advertising Agencies (AAAA) have provided suggested language for proposed Regulation 1540.

After analyzing the AAAA's proposed language, it appears that AAAA is combining the old format and the new format as recommended by staff, in addition to providing new interpretations of:

- Clip-art. AAAA proposes that clip-art be considered an intermediate production aid. (Exhibit 4, subdivision (a)(8).)
- Preliminary art. AAAA proposes that preliminary art be regarded as incidental to the true object of the transaction. (Exhibit 4, subdivision (a)(10).)

A separate analysis of the AAAA's suggested language has been made in Exhibit 4. The AAAA's recommendation has no operative date.

AAAA proposes language that it believes provides a more "user friendly" regulation without undue complexity. They have incorporated some of staff's recommended changes and have provided alternative language. AAAA believes that staff's new version is more complex than the previous draft and are of the opinion that the existing regulation is quite satisfactory to the industry.

AAAA's proposal has no operative date and is shown in Exhibit 4.

B. Pros of the Alternative

Reflects the views of AAAA.

C. Cons of the Alternative

- Requires regulatory change.
- Is inconsistent with the gross receipts provisions established by statute.
- Would return to confusing organization of the current version.
- Is contrary to the stated position of AAAA that the current version is satisfactory in that it would incorporate those changes proposed by staff which AAAA views as favorable as well as proposing additional changes.

D. Statutory or Regulatory Change

Statutory change required to treat the transfers of preliminary art in tangible form as incidental to the conceptual and design services provided. This alternative does require amendments to Regulation 1540.

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E. Administrative Impact

Staff will be required to notify taxpayers of the amendments to the regulation through an article in the Tax Information Bulletin. In addition, revisions to various procedures manuals and Board publications may be needed.

F. Fiscal Impact

1. Cost Impact

No additional cost. Staff will notify taxpayers of the regulation amendments through a Tax Information Bulletin (TIB) article. The workload associated with publishing and distributing the TIB is considered routine and any corresponding cost would be within the Board's existing budget. Similarly, the workload associated with revising procedure manuals and Board publications is considered routine and any corresponding cost would be within the Board's existing budget.

2. Revenue Impact

See Revenue Estimate (Exhibit 1).

G. Taxpayer/Customer Impact

Allows inconsistent application of tax in regard to transfers of digital files with the provisions of Regulation 1502, which excludes from tax only programs or files transferred through remote telecommunications.

H. Critical Time Frames

The proposed amendments represent interpretations of existing statutes, and therefore have no operative date. Implementation will take place 30 days following approval of the regulation by the Office of Administrative Law.

XI. Alternative 6

A. Description of the Alternative

Mr. Patrick Leone, CPA, proposes that the terminology "ultimately subject to sales tax" as used in Regulation 1541 not be replaced. In addition, if the phrase is deleted, Mr. Leone proposes that the change be applied on a prospective basis. Mr. Leone believes that this language clearly exempts resales, which are ultimately sold and taxed. By changing this wording to be more restrictive, Mr. Leone believes that the meaning of the regulation will significantly change and thereby, will take away a tax benefit previously given to printers.

Mr. Leone believes that the phrase "ultimately subject to sales tax" is clear in its meaning. If printed matter is ultimately (eventually, lastly, in the end) subject to tax, the special printing aids are included in the lump-sum sale price and can be purchased ex-tax. According to Mr. Leone, many printers have accrued tax only on printing aids that related to out of state sales or other exempt sales. Therefore, Mr. Leone proposes that if any change to the regulatory language is made, that the change be on a prospective basis in an effort to not penalize the printers that relied on the plain reading of the regulation.

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According to Mr. Leone, the language is more restrictive because it requires printers to separately state printing aids on their invoice in order to sell for resale, in addition to obtaining a resale certificate for the printing aids. Mr. Leone also takes issue with staff's newly added language to clarify the application of tax to special printing aids when a printer sells the printed matter to multiple purchasers. Staff added this subdivision, (c)(2)(B)1., to address one area of confusion that arose from the current language of Regulation 1541.

Mr. Leone's proposal is shown in Exhibit 6.

B. Pros of the Alternative

Does not require regulatory change.

C. Cons of the Alternative

- Continues to cause confusion regarding the interpretation of the phrase "ultimately subject to tax."
- Does not clarify the application of tax to special printing aids.
- Would fail to clearly reflect staff's interpretation and application of the current provision in the regulation using terminology that would avoid the confusion that proponent's position acknowledges.

D. Statutory or Regulatory Change

No statutory or regulatory change required.

E. Administrative Impact

None. In addition, revisions to various procedures manuals and Board publications may be needed.

F. Fiscal Impact

1. Cost Impact

No additional cost. Staff will notify taxpayers of the regulation amendments through a Tax Information Bulletin (TIB) article. The workload associated with publishing and distributing the TIB is considered routine and any corresponding cost would be within the Board's existing budget. Similarly, the workload associated with revising procedure manuals and Board publications is considered routine and any corresponding cost would be within the Board's existing budget.

2. Revenue Impact

See Revenue Estimate (Exhibit 1).

G. Taxpayer/Customer Impact

Taxpayers will continue to request clarification on transactions involving special printing aids "ultimately subject to tax" or otherwise.

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H. Critical Time Frames

The proposed amendments represent interpretations of existing statutes, and therefore have no operative date. Implementation will take place 30 days following approval of the regulation by the Office of Administrative Law. However, if staff's recommendation is adopted, then the proposed amendments to Regulation 1541 will have an operative date of October 1, 2002.

Prepared by: Program Planning Division, Sales and Use Tax Department

Current as of: 1/25/02

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Graphic Arts Issue Paper

List of Exhibits

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Regulation 1540 –AAAA’s Proposed Language	Exhibit 4
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**PROPOSED REGULATORY CHANGES REGARDING
APPLICATION OF TAX TO GRAPHIC ARTS AND RELATED
ENTERPRISES
(REGULATIONS 1540, 1541, 1543 AND 1528)**

Recommendation and Alternatives

Staff Recommendation:

Staff recommends the adoption of amendments to Regulations 1540, 1541, 1543, and 1528 as provided in Exhibits 5, 7, 8 and 9 of the issue paper. Staff's recommendations have no operative date.

Alternative 1:

In addition to staff's recommendation, Mr. Eric Miethke representing the Graphic Artists Guild (Guild), proposes amendments to Regulation 1540 as provided in Exhibit 3 of the issue paper. The Guild's proposal recommends no operative date.

Alternative 2:

In addition to staff's recommendation, Mr. Nicholas Blonder, Attorney at Law, proposes amendments to Regulation 1540 as provided in Exhibit 3 of the issue paper. Mr. Blonder's proposal recommends no operative date.

Alternative 3:

In addition to staff's recommendation, Mr. Don Wayne proposes amendments to Regulation 1540 as provided in Exhibit 3 of the issue paper. Mr. Wayne's proposal recommends no operative date.

Alternative 4:

In addition to staff's recommendation, Mr. Peter Liao proposes amendments to Regulation 1540 as provided in Exhibit 3 of the issue paper. Mr. Liao's proposal recommends no operative date.

Revenue Estimate**Alternative 5:**

Mr. Don Jung and Mr. Joseph Vinatieri, representing the American Association of Advertising Agencies (AAAA), propose amendments to Regulation 1540 as provided in Exhibits 3 and 4 of the issue paper. The AAAA's proposal recommends no operative date.

Alternative 6:

As proposed by Mr. Patrick Leone, CPA, adopt staff's recommendation except do not replace the language "ultimately subject to sales tax" in Regulation 1541(c)(1) as provided in Exhibit 6 of the issue paper. If staff's recommendation is approved, Mr. Leone recommends an operative date of October 1, 2002.

Background, Methodology, and Assumptions**Staff Recommendation:**

The staff recommendation would not impact revenues.

The staff recommendation would incorporate the findings in the California Supreme Court decision in *Preston vs. State Board of Equalization*. The portion of the proposed regulation that deals with the findings in this case would have no revenue impact as any change in revenue is caused by the court decision and would occur regardless of this regulation.

As a point of information, the revenue impact of the April 2, 2001 California Supreme Court decision, *Preston v state Board of Equalization* is estimated to amount to \$57.7 million annually. This estimate is based on a study of sales and use tax returns of advertising agencies, and commercial artists and designers conducted in conjunction with a legislative proposal that would have specified that for sales and use tax purposes "sale" and "purchase" do not include the granting of a right to reproduce or copy a two- or three- dimensional image.

The staff recommendation would also implement the provisions of Senate Bill 330, chapter 799 (1999) that provides an exclusion from "sale" or "purchase" for certain transfers of original drawing, sketches, illustrations or paintings by artists or designers at a social gathering. The portion of the proposed regulatory changes that deals with such provisions would have no revenue impact as any change in revenue is caused by the passage of SB 330.

The other provisions of the staff recommendation would clarify the language in the current regulations, would not change current practice and would therefore not result in any revenue impact.

Alternatives:

Section 6011(c)(10)(C) of the Revenue and Taxation Code provides that if the technology transfer agreement does not separately state a price for the tangible personal property, and the tangible personal property or like tangible personal property has not been previously sold or leased, or offered for sale or lease, to third parties at a separate price, the retail fair market value shall be equal to 200 percent of the cost of materials and labor used to produce the tangible personal property subject to tax. Most of the provisions of the various alternatives that would impact revenues deal with those transactions that would require a retail fair market value calculation. The retail fair market value calculation would be required only for a portion of the total number of technology transfer agreements. We have no way of knowing what this portion might be. Since the court decision is so recent, the Board has no audit experience to help us

Revenue Estimate

estimate what percentage of these technology transfer agreements will separately state a price for the tangible personal property.

The sales tax study done for the legislative proposal on the taxability of reproduction rights resulted in an estimate of \$611.7 million in annual sales of reproduction rights by advertising agencies, commercial artists and designers, and commercial photographers. These sales are now exempt pursuant to the court decision. If we assume that this amount represents 90% of the total sales of finished artwork sold with reproduction rights and that the remaining 10% represents the sale of tangible personal property, then the total sales of tangible personal property would amount to \$68 million annually. The total state and local sales and use tax revenues on this amount would be \$5.4 million. If we further assume that one-quarter of this amount represents transactions that require a calculation of fair market value, there would be a separately stated price for the tangible personal property transferred in the remaining transactions. This would mean that the total annual revenue that would be subject to a fair market value calculation is estimated to be \$1.3 million. For the fair market value calculation, it is assumed that the cost of materials would comprise 10% of the calculation, and labor would comprise 90%. In terms of sales and use tax revenue, the amounts are estimated to be \$100,000 for cost of materials and \$1.2 million for labor costs.

Alternative 1:

Alternative 1 includes two proposed changes to Regulation 1540 that impact revenues. The first would provide that finished artwork temporarily transferred on computer storage media in a technology transfer agreement has a de minimus fair rental value and the value of the artwork is incidental to the transfer of the intangible rights. This proposed change would provide that no sales tax would be due on such transactions. This would result in a loss of revenue. However, since these transactions represent just a small portion of the \$1.3 million in sales and use tax revenues enumerated above, this loss would be minimal.

The other proposed change would provide that the value of the labor provided by the artist should not be included in the calculation of the measure of tax in those instances where there is a technology transfer agreement and a separate price for the tangible personal property is not stated. The loss of revenue due to this provision will depend on the portion of the labor cost that is due to the artist's own labor. If the artist's own labor is a significant portion of the labor costs, then the revenue loss will be a significant portion of the \$1.2 million in sales and use tax revenues enumerated above.

Alternative 2:

The provision of Alternative 2 that would have a revenue impact is the same cost of labor issue as in Alternative 1, namely, whether or not the artist's own labor should be included in the measure of tax. The loss of revenue due to this provision will depend on the portion of the labor cost that is due to the artist's own labor. If the artist's own labor is a significant portion of the labor costs, then the revenue loss will be a significant portion of the \$1.2 million in sales and use tax revenues enumerated above.

Alternative 3:

Alternative 3 has no revenue effect.

Revenue Estimate**Alternative 4:**

The provision of Alternative 4 that would impact revenue is the provision that would provide that the cost of materials only consists of those materials physically incorporated into the finished art. This would mean that such items as intermediate production aids, photographs and other tangible personal property would not be included in the calculation of fair market value. This would result in a revenue loss. However, since this is just a portion of the \$100,000 enumerated above, this loss would be minimal.

Alternative 5:

Alternative 5 would provide that preliminary art be regarded as incidental to the true object of the transaction and would, therefore, not be subject to tax. Currently, preliminary art is not considered to be taxable unless title or permanent possession of the preliminary artwork is transferred to the client. It is not clear whether or not the provisions of Alternative 5 would constitute a change to this policy. To the extent that the provisions of Alternative 5 do make some currently taxable transfers of preliminary art not subject to tax, there would be a revenue loss. Unfortunately, there is no information available on the current amount of sales and use tax revenue collected on transfers of preliminary art.

Alternative 6:

Alternative 6 has no revenue effect.

Revenue Summary**Staff Recommendation:**

The staff recommendation has no revenue effect.

Alternative 1:

Alternative 1 would result in a loss of sales and use tax revenue. The amount of that loss would be some portion of the estimated \$1.3 million in sales and use tax revenue that would be collected on technology transfer agreements for which a fair market value calculation is required.

Revenue Estimate

Alternative 2:

Alternative 2 would result in a loss of sales and use tax revenue. The amount of that loss would be some portion of the estimated \$1.3 million in sales and use tax revenue that would be collected on technology transfer agreements for which a fair market value calculation is required.

Alternative 3:

Alternative 3 has no revenue effect.

Alternative 4:

Alternative 4 would result in a minimal revenue loss.

Alternative 5:

Alternative 5 could result in a revenue loss to the extent that preliminary art that is currently subject to sales and use tax would no longer be taxable.

Alternative 6:

Alternative 6 has no revenue effect.

Preparation

This revenue estimate was prepared by David E. Hayes, Research and Statistics Section, Agency Planning and Research Division. This revenue estimate was reviewed by Ms. Margaret Shedd, Legislative Counsel and Ms. Charlotte Paliani, Program Planning Manager, Sales and Use Tax Department. For additional information, please contact Mr. Hayes at (916) 445-0840.

Current as of January 24, 2002

Regulation 1540. Advertising Agencies, Commercial Artists and Designers.

Reference: Sections 6006, 6010.3 and 6015, Revenue and Taxation Code.

(a) Advertising Agencies.

(1) General. Advertising agencies provide clients with both services and tangible personal property. Services include, without limit, consultation, consumer research, and media placement. Tangible personal property includes, without limit, video and audio productions, print advertisements, brochures, finished artwork, and other printed matter. When an advertising agency provides services unrelated to the transfer of tangible personal property or when the tangible personal property transferred is incidental to the services, the charges for those services are nontaxable.

Application of tax to the sale of tangible personal property and any services related to the sale is dependent on the type of property being sold and the relationship of the advertising agency to the client.

(2) Specific Situations.

(A) Electronic or Digital Artwork. Electronic or digital art is the process of using computer software and hardware to compile or compose finished art. Elements of the process include: creation of original artwork or photographs, scanning of artwork or photographs, composition and design of text, insertion and manipulation of scanned and original digital artwork, photographs, or text.

A transfer of electronic or digital art from an advertising agency, commercial artist or designer to a client or to a third party on behalf of a client that includes text or images or a combination of both, is not taxable if, (1) the file containing the electronic or digital art is transferred through remote telecommunications, such as a modem, or (2) the file is downloaded on the client's computer by the advertising agency, commercial artist or designer and the client does not obtain title to or possession of any tangible personal property, such as a diskette or compact disk. The advertising agency, commercial artist, or designer should document the downloading of electronic artwork in the manner set forth in subdivision (d)(2). Transfer of a file qualifying as electronic or digital pre-press instruction as defined by the provisions of Regulation 1541, Printing and Related Arts, is nontaxable.

A transfer of title to or possession of a file on electronic media, such as a diskette or compact disc, is subject to tax as stated in subdivision (d)(2).

(B) Agency Acting as an Agent for Its Client. An agent is one who represents another, called the principal, in dealings with third persons. (Civil Code, Section 2295.) To the extent an advertising agency acts as an agent of its client in acquiring tangible personal property, it is neither a purchaser of the property with respect to the supplier nor a seller of the property with respect to its principal. Because of the unique relationship between advertising agencies and

Current Language

Regulation 1540.

Advertising Agencies, Commercial Artists and Designers.

clients, it is rebuttably presumed that an advertising agency qualifies as an agent when acquiring tangible personal property on behalf of its client. However, an agency is not an agent of its client with respect to tangible personal property fabricated or produced in-house by the agency's own employees and sold to its client.

As an agent for its client, sales or use tax is due on the purchase price from the suppliers to the advertising agency. Tax does not apply to the charge made by an advertising agency to its client for reimbursement, including tax reimbursement, charged by a supplier or to charges or fees for an agency's services directly related to such acquisitions of tangible personal property.

An advertising agency may not issue a resale certificate when making purchases as an agent. It will be presumed that an advertising agency who issues a resale certificate to a supplier is purchasing tangible personal property on its own behalf for resale and is not acting as an agent for its client. However, the advertising agency may provide evidence to prove that the presentation of the resale certificate was erroneous and that the advertising agency was acting as an agent of its client. If the resale certificate was issued in error, the advertising agency is liable for use tax on the cost of tangible personal property purchased under the certificate unless, 1. The agency has already paid tax to the supplier or to the Board, or 2. The client has self-reported the tax.

(3) Advertising Agencies Acting as Retailers.

(A) Election of Non-Agent Status. An advertising agency may elect non-agent status with respect to sales to its client. This election must be supported by a specific written statement in its contract or agreement with the client. Alternatively, a statement may be included on an agency's invoice to its client. Statements should include the following or similar language: "(Agency name) does not qualify as an agent of (client name) for purposes of this transaction."

An agency that elects non-agent status is a retailer with respect to tangible personal property sold to its clients. The agency may issue a resale certificate to its suppliers for tangible personal property that it is planning to resell to clients or to incorporate into property that will be sold to clients.

The taxable selling price is the separately stated charge for the tangible personal property. If there is no separately stated charge, the taxable selling price may be calculated as shown in subdivision (b).

(B) Items Produced or Fabricated by an Agency In-House. Advertising agencies are retailers of tangible personal property produced or fabricated by their own employees. Advertising agencies are not agents of their clients with respect to the acquisition of materials incorporated into items of tangible personal property prepared by their employees. However, in the case of intermediate production or printing aids used by the agency's employees to fabricate tangible personal property, it will be presumed that an advertising agency passes title to the aids to the client prior to use by the agency and the measure of tax will be computed in the same manner as provided in Regulation 1541 for special printing aids. Intermediate production or printing aids

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include, but are not limited to, artwork, illustrations, photography, photo engravings, and other similar materials.

Except for artwork, tax is due on the taxable selling price of tangible personal property fabricated or produced by the agency's employees. Artwork shall be taxed in the manner set forth in subdivision (b)(1) or (d). An advertising agency should issue a resale certificate for items that become an ingredient or component part of such tangible personal property and for intermediate production or printing aids. The term "ingredient or component part of other tangible personal property" includes only those items that become physically incorporated into the property and not those which are merely consumed or used in the production of the property sold.

(b) Lump-Sum Sales of Tangible Personal Property.

(1) An agency that has a contract or agreement to sell tangible personal property for a lump-sum amount is a retailer of the tangible personal property and tax applies to the lump-sum selling price, except for artwork. An advertising agency, commercial artist or designer making a lump-sum sale of tangible personal property to a client may issue a resale certificate to a supplier.

On sales of artwork for which an advertising agency, commercial artist or designer makes a lump-sum charge that includes both the nontaxable services defined in subdivision (d)(1) and finished art, it will be rebuttably presumed that 75% of the lump-sum charge is for the nontaxable services.

(2) Taxable Selling Price. If advertising agencies, commercial artists or designers combine charges for nontaxable services, such as media placement, with the charges for tangible personal property of which the agencies, artists or designers are the retailers, they shall report a "taxable selling price" for the tangible personal property that includes the total of: 1. direct labor, 2. the cost of purchased items that become an ingredient or component part of the tangible personal property and the cost of any intermediate production or printing aids, and 3. a reasonable markup. An advertising agency, commercial artist or designer must keep sufficient records to document the basis for the reported taxable selling price.

(3) Specific Nontaxable Charges. The following and similar fees, commission, and services are nontaxable if separately stated. If not separately stated, these charges are not considered direct labor when calculating a taxable selling price as defined in subdivision (b)(2).

(A) Agent fees added to purchases of tangible personal property by agencies established as agents for their clients as compensation for their performances of services related to such purchases.

(B) Media commissions derived by agencies for placement of advertising whether paid by the medium, by another agency, or by the client. The service of placing of advertising is not a service that is a part of a sale of tangible personal property.

(C) Commissions paid to agencies by suppliers. Examples of such commissions are those paid to an agency by a premium manufacturer (or distributor) or a direct-by-mail supplier.

(D) Consultation and concept development fees related to client discussion, development of ideas and other services. Tangible personal property produced as a result of these services is incidental to the service and nontaxable.

(E) Research or account planning that entail consumer research and the application of that research to the client's business or industry.

(F) Quality control supervision that entails the proofing and review of printing and other products provided by outside vendors.

(G) Separately stated charges for the formulation and writing of copy.

(4) Taxable Charges for Agencies Acting as Retailers. ~~Specific Applications.~~ All other commissions, fees or services exclusively related to the production or fabrication of tangible personal property are taxable and are considered part of direct labor. Such charges include retouching of photographs or other artwork for reproduction, provided the retouching is intended to improve the quality of the reproduction. Retouching for the purpose of repairing or restoring a photograph to its original condition is not taxable.

(5) Charges and Transactions Governed by Other Regulations.

(A) Video or Film Productions. If video or film productions provided by an advertising agency to clients are qualified production services, the application of tax is determined by Regulation 1529, *Motion Pictures*.

(B) Audio Productions. An audio production provided by an advertising agency to a client falls under the provisions of Regulation 1527, *Sound Recording*. Tax will apply as defined by that regulation.

(C) Typography. Tax applies to charges for typography or composed type obtained from outside vendors as provided in Regulation 1541, *Printing and Related Arts*.

(c) Commercial Artists and Designers.

General. Commercial artists and designers provide services, electronic artwork, and tangible personal property to their clients. Services include, but are not limited to, the creation and development of ideas, concepts, looks, or messages. Electronic artwork can be transferred either through remote telecommunications, such as a modem, or by electronic media such as diskettes or compact disks. Tangible personal property includes both electronic media on which electronic artwork is transferred to the client and hard copies of the electronic artwork, or manually created art. "Finished art" means the final art used for actual reproduction by

photomechanical or other processes, or used for display. It includes, but is not limited to, electronic art, illustrations (e.g. drawings, diagrams, halftones, or color images), photographs, paintings, and handlettering. Blueprints, diagrams, and instructions for signage furnished to a client as the result of environmental graphic design services are not “finished art.”

An advertising agency that provides creative or development services for the sole purpose of furnishing finished art to their clients is subject to tax as provided in subdivision (d).

(d) Application of Tax to Commercial Artists, Designers and Advertising Agencies.

(1) Services. Services performed to convey ideas, concepts, looks or messages to a client may result in a transfer, enhancement or revision of either electronic artwork, hard copies of electronic artwork, or copies of manually prepared artwork. If charges for such services are separately stated as “design charges,” “preliminary art,” “concept development,” or any other designation that clearly indicates that the charges are for such services and not for finished art, they are nontaxable unless the contract of sale provides that the commercial artist or designer or advertising agency will pass to the client title or the right to permanent possession of the electronic media or hard copy.

A commercial artist or designer or advertising agency who provides nontaxable services is the consumer of tangible personal property used in the performance of such services and tax applies to the sale of property to the commercial artist or designer or advertising agency.

(2) Electronic Artwork and Finished Art. A transfer of electronic artwork from a commercial artist or designer or advertising agency to a customer or to a third party on behalf of the customer is not taxable if the file containing the electronic artwork is transferred through remote telecommunications, or if the file is loaded on the customer’s computer by the commercial artist or designer or advertising agency, and the customer does not obtain title to or possession of any tangible personal property, such as electronic media. The graphic artist or advertising agency should document his or her transfer and loading of electronic artwork on the client’s computer by a statement on the invoice or contract with the following language: “This electronic artwork was loaded onto my computer by (graphic artist’s or seller’s name). No electronic media, such as diskettes or compact disks, or hardcopies containing the artwork were transferred to me.” This statement should be signed or initialed by the client. When such a statement is timely completed, it will be rebuttably presumed that the transfer of electronic artwork is nontaxable. To be timely completed, the statement must be initialed or signed at the time the file is loaded or at the point the transfer is invoiced to the client. In lieu of the statement, the commercial artist or designer or advertising agency may provide other substantive evidence indicating that the artwork was transferred in an exempt manner.

The electronic or manual preparation of finished art for use in reproduction or display is not a service. Unless transferred or installed in the manner set forth in the preceding paragraph, tax applies to all charges for finished art, including to all charges for any rights, as provided in subdivision (d)(4), sold with the finished art, such as, without limitation, copyrights or distribution and production rights. If charges for finished art are combined with nontaxable

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services described in subdivision (d)(1), tax may be reported on a calculated selling price, as defined in subdivision (b)(2) provided the retail selling price also includes the value of rights as provided in subdivision (d)(4). In lieu of using a calculated selling price, commercial artists and designers or advertising agencies may use the method described in (b)(1), that is, it will be rebuttably presumed that 75% of a combined charge is for the nontaxable services.

If the commercial artist or designer or advertising agency uses any intermediate production or printing aids in the creation of the finished art, it will be presumed that title to the aids was passed to the client prior to use by the commercial artist or designer or advertising agency. The measure of tax for these aids will be computed in the same manner as provided by Regulation 1541 for special printing aids. Intermediate production or printing aids include, but are not limited to, artwork, illustrations, photography, photo engravings, and other similar materials.

(3) Signage. Tax does not apply to the services to create single copies of blueprints, diagrams, and instructions for signage provided as a result of environmental graphic design. Reproduction charges for additional copies are taxable.

(4) Reproduction Rights. Charges for the transfer by a tangible medium of a photograph or of finished art for purposes of reproduction are taxable even though there is no transfer of title to the person reproducing the photograph or work of art. Charges for the right to use the photograph or finished art which has been transferred by tangible medium in the production of tangible personal property are taxable. Charges for a license, copyright, or subpart of a copyright (such as a right to reproduce or to prepare derivative works) to exploit the photograph or finished art are taxable if they are sold along with the photograph or finished art transferred by tangible media or they are sold by a subsequent contract entered into within one year of the original transfer of the photograph or finished art.

Tax does not apply to a sale of an additional license, copyright, or the subpart of a copyright, or to the receipt of royalties received from the exploitation of a copyright, or subpart thereof, if such sale or receipt of royalties occurs more than one year from the date of the original transfer of the physical media containing the photograph or work of art so exploited. Such copyrights or royalties are not considered to have been sold along with finished art transferred by tangible media for the purposes of this subdivision and are deemed sales of nontaxable intangible property.

This limitation does not apply to sales or transfers for reproduction by a subsequent owner of the photograph or finished art, such as a stock photo or stock artwork house; however, where the stock photo or stock artwork house is merely acting as an agent for the original artist or photographer, the above limitation applies.

(5) Websites. The design, editing or hosting of an electronic website in which no tangible personal property is transferred to the customer is not subject to tax.

(e) Items Purchased by an Advertising Agency or by an Artist or Designer. An advertising agency, or commercial artist, or designer is the consumer of tangible personal property used in

the operation of its business. Tax applies to the sale of such property to the agency, artist, or designer.

Proposed Regulatory Changes Regarding Application of Tax to Graphic Arts and Related Enterprises
Comparison of Proposed Language for Regulation 1540
Current as of January 16, 2002

Action Item *	Regulatory Language Proposed by Staff	Regulatory Language Proposed by Guild (Alternative 1)	Regulatory Language Proposed by Blonder (Alternative 2)	Regulatory Language Proposed by Wayne (Alternative 3)	Regulatory Language Proposed by Liao (Alternative 4)	Regulatory Language Proposed by AAAA (Alternative 5)
ACTION 2 - Organization of Regulation	<i>Note – Staff provided revised language to interested parties on 12-19-01.</i>	<i>Note – Alternative language is on pages 23-27.</i>	<i>Note – Alternative language is on pages 25-26.</i>	<i>Note – Alternative language begins on page 7 and continues throughout table.</i>	<i>Note – Mr. Liao did not respond to staff's revised language. Alternative language is on pages 23-27.</i>	
	Regulation 1540. ADVERTISING AGENCIES AND COMMERCIAL ARTISTS AND DESIGNERS.	Regulation 1540. ADVERTISING AGENCIES AND COMMERCIAL ARTISTS AND DESIGNERS.	Regulation 1540. ADVERTISING AGENCIES AND COMMERCIAL ARTISTS AND DESIGNERS.	Regulation 1540. ADVERTISING AGENCIES AND COMMERCIAL ARTISTS AND DESIGNERS.	Regulation 1540. ADVERTISING AGENCIES AND COMMERCIAL ARTISTS AND DESIGNERS.	AAAA proposes an organization for Regulation 1540 that is different from staff's and other alternatives. The primary difference is the reversal of major sections (b) and (c). Regulation 1540. ADVERTISING AGENCIES AND COMMERCIAL ARTISTS AND DESIGNERS.
ACTION 21 - General Language Differences	(a) DEFINITIONS. (1) ADVERTISING. Advertising is commercial communication utilizing one or more forms of communication (such as television, print, billboards, or the Internet) from or on behalf of an identified person to an intended target audience.	(a) DEFINITIONS. [same as staff's]	(a) DEFINITIONS. [same as staff's]	(a) DEFINITIONS. [same as staff's]	(a) DEFINITIONS. [no comments received]	(a) DEFINITIONS. (1) ADVERTISING. Advertising is commercial communication utilizing one or more forms of communication (such as television, print, billboards, or the Internet) from or on behalf of an identified person or entity to an intended target audience.
	(2) ADVERTISING AGENCIES. Advertising agencies design and	[same as staff's]	[same as staff's]	[same as staff's]	[no comments received]	(2) ADVERTISING AGENCIES. Advertising agencies design and

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Proposed Regulatory Changes Regarding Application of Tax to Graphic Arts and Related Enterprises
Comparison of Proposed Language for Regulation 1540
Current as of January 16, 2002

Action Item *	Regulatory Language Proposed by Staff	Regulatory Language Proposed by Guild (Alternative 1)	Regulatory Language Proposed by Blonder (Alternative 2)	Regulatory Language Proposed by Wayne (Alternative 3)	Regulatory Language Proposed by Liao (Alternative 4)	Regulatory Language Proposed by AAAA (Alternative 5)
ACTION 21 - General Language Differences	implement advertising campaigns for purposes of advertising the goods, services, or ideas of their clients. As part of that primary function, advertising agencies provide their clients with services (such as consultation, consumer research, media planning and placement, public relations, and other marketing activities) and tangible personal property (such as print advertisements, finished art, and video and audio productions).					implement advertising campaigns for purposes of advertising the goods, services, or ideas of their clients. As part of that primary function, advertising agencies provide their clients with services (such as consultation, consumer research, and media placement, television and radio commercials, print advertising, brand advertising, website design, internet design, public relations and development of marketing, communication programs) and tangible personal property (such as print advertisements, finished art, and video and audio productions). Incidental to these services, the advertising agencies may provide some tangible personal property to the client.
ACTION 21 - General Language Differences	(3) COMMERCIAL ARTISTS. Commercial artists, who may characterize themselves as commercial artists, commercial photographers, or	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[no comments received]</i>	(3) COMMERCIAL ARTISTS AND DESIGNERS. <i>[same as staff's]</i>

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Proposed Regulatory Changes Regarding Application of Tax to Graphic Arts and Related Enterprises
Comparison of Proposed Language for Regulation 1540
 Current as of January 16, 2002

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	designers, provide services and tangible personal property to their clients for use in their clients' advertising campaigns, or for their clients' other commercial endeavors such as sales of copies of finished art (including, e.g., photographic images) provided by a commercial artist. Services they provide to their clients include the creation and development of ideas, concepts, looks, or messages. Electronic artwork they provide may be transferred through remote telecommunications such as by modem or over the Internet, or by tangible means through electronic media such as compact or floppy disc. Tangible personal property they provide may include electronic media on which electronic artwork is transferred to the client, hard copies of the electronic artwork, hard copies of finished art (which may consist of photographic images).					

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Proposed Regulatory Changes Regarding Application of Tax to Graphic Arts and Related Enterprises
Comparison of Proposed Language for Regulation 1540
 Current as of January 16, 2002

Action Item *	Regulatory Language Proposed by Staff	Regulatory Language Proposed by Guild (Alternative 1)	Regulatory Language Proposed by Blonder (Alternative 2)	Regulatory Language Proposed by Wayne (Alternative 3)	Regulatory Language Proposed by Liao (Alternative 4)	Regulatory Language Proposed by AAAA (Alternative 5)
ACTION 4 – Definition of Contract of Sale	(4) CONTRACT OF SALE. An agreement to transfer tangible personal property for consideration is a contract of sale. A contract of sale consists of all terms comprising the obligation of the parties for the sale and purchase of the tangible personal property in question. A contract of sale may consist of a single contract document. A contract of sale may also consist of multiple documents. For example, a master agreement between an advertising agency and its client may specify the obligations of each with respect to the design of an advertising campaign for the client, the placement of the advertising with print and television media, and for the sale and purchase of tangible personal property related to the advertising campaign. There may then be additional terms for the purchase of specific tangible personal property during the advertising campaign, such as in a purchase order, which identifies the	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[no comments received]</i>	(4) CONTRACT OF SALE. An agreement to transfer tangible personal property for consideration is a contract of sale. A contract of sale consists of all terms comprising the obligation of the parties for the sale and purchase of the tangible personal property in question. A contract of sale may consist of a single contract document. A contract of sale may also consist of multiple documents. For example, a master agreement between an advertising agency and its client may specify the obligations of each with respect to the design of an advertising campaign for the client, the placement of the advertising with print and television media, and for the sale and purchase of tangible personal property related to the advertising campaign. There may then be additional terms for the purchase of specific tangible personal property during the advertising campaign, such as in a purchase order, which identifies the

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Proposed Regulatory Changes Regarding Application of Tax to Graphic Arts and Related Enterprises
Comparison of Proposed Language for Regulation 1540
 Current as of January 16, 2002

Action Item *	Regulatory Language Proposed by Staff	Regulatory Language Proposed by Guild (Alternative 1)	Regulatory Language Proposed by Blonder (Alternative 2)	Regulatory Language Proposed by Wayne (Alternative 3)	Regulatory Language Proposed by Liao (Alternative 4)	Regulatory Language Proposed by AAAA (Alternative 5)
ACTION 3 – New Clarifying Language (Definition of Digital Pre- Press Instruction)	specific property that will be purchased and sold and the sales price for that property. In this example, not all terms of the sale and purchase of the tangible personal property identified in the purchase order are included in the master agreement, nor are all terms included in the purchase order. Rather, the contract of sale in this circumstance consists of the relevant provisions of the master agreement as modified by the specific provisions in the purchase order. <u>(5) DIGITAL PRE-PRESS INSTRUCTION. Digital pre-press instruction is the creation of original information in electronic form by combining more than one computer program into specific instructions or information necessary to prepare and link files for electronic transmission for output to film, plate, or direct to press, which is then transferred on electronic media such as tape or compact disc.</u>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	specific property that will be purchased and sold and the sales price for that property. In this example, not all terms of the sale and purchase of the tangible personal property identified in the purchase order are included in the master agreement, nor are all terms included in the purchase order. Rather, the contract of sale in this circumstance consists of the relevant provisions of the master agreement as modified by the specific provisions in the purchase order. <i>[no comments received – staff added language after final interested parties submissions were received]</i>

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Proposed Regulatory Changes Regarding Application of Tax to Graphic Arts and Related Enterprises
Comparison of Proposed Language for Regulation 1540
 Current as of January 16, 2002

Action Item *	Regulatory Language Proposed by Staff	Regulatory Language Proposed by Guild (Alternative 1)	Regulatory Language Proposed by Blonder (Alternative 2)	Regulatory Language Proposed by Wayne (Alternative 3)	Regulatory Language Proposed by Liao (Alternative 4)	Regulatory Language Proposed by AAAA (Alternative 5)
ACTION 21 – General Language Differences	(6) ELECTRONIC ARTWORK. Electronic artwork is artwork created through the use of computer hardware and software processes which results in artwork in a digital format that can be transmitted to others via electronic means (that is, transmitted through remote telecommunications such as by modem or over the Internet, or by electronic media such as compact or floppy disc). Elements of the process include the creation of original artwork or photographic images, scanning of artwork or photographic images, composition and design of text, insertion and manipulation of scanned and original electronic artwork, photographic images, and text. Electronic artwork does not include artwork that is transferred to clients in a tangible form, other than on electronic media, even where such artwork may have been manufactured or produced in whole or in part by computer hardware and	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[no comments received]</i>	(5) ELECTRONIC ARTWORK. Electronic artwork is artwork created through the use of computer hardware and software processes which results in artwork in a digital format that can be transmitted to others the client or a third party via electronic means (that is, transmitted through remote telecommunications such as by modem or over the Internet, or by electronic media such as compact or floppy disc). Elements of the process include the creation of original artwork or photographic images, scanning of artwork or photographic images, composition and design of text, insertion and manipulation of scanned and original electronic artwork, photographic images, and text. Electronic artwork does not include artwork that is transferred to customers in a tangible form, such as compact or floppy disc. other than on electronic media, even where such artwork may have been manufactured
ACTION 21 – General Language Differences						

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Proposed Regulatory Changes Regarding Application of Tax to Graphic Arts and Related Enterprises
Comparison of Proposed Language for Regulation 1540
 Current as of January 16, 2002

Action Item *	Regulatory Language Proposed by Staff	Regulatory Language Proposed by Guild (Alternative 1)	Regulatory Language Proposed by Blonder (Alternative 2)	Regulatory Language Proposed by Wayne (Alternative 3)	Regulatory Language Proposed by Liao (Alternative 4)	Regulatory Language Proposed by AAAA (Alternative 5)
ACTION 5 - Definition of Finished Art	software processes.					or produced in whole or in part by computer hardware and software processes.
	(7) FINISHED ART. Finished art is the final artwork used for actual reproduction by photomechanical or other processes, or used for display. It includes electronic artwork, illustrations (e.g. drawings, diagrams, halftones, or color images), photographic images, sculptures, paintings, and handlettering. Blueprints, diagrams, and instructions for signage furnished to a client as the result of environmental graphic design services are not finished art. <i>[Interested parties have indicated concurrence with staff's proposed language for subdivision (a)(8) – see Exhibit 5, page 2.]</i>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	(7) FINISHED ART. Finished art is the final artwork used for actual reproduction by photomechanical or other processes, such as preparation of special printing aids , or used for display. It includes electronic artwork, illustrations (e.g. drawings, diagrams, halftones, or color images), photographic images, sculptures, paintings, and handlettering. Blueprints, diagrams, and instructions for signage furnished to a client as the result of environmental graphic design services are not finished art.	<i>[no comments received]</i>	(6) FINISHED ART. Finished art is the final artwork used for actual reproduction by photomechanical or other processes, or used for display. It includes electronic artwork, illustrations (e.g. drawings, diagrams, halftones, or color images), photographic images, sculptures, paintings, and handlettering. Blueprints, diagrams, and instructions for signage furnished to a client as the result of environmental graphic design services or advertising agencies are not finished art.
ACTION 21 – General Language Differences						

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Proposed Regulatory Changes Regarding Application of Tax to Graphic Arts and Related Enterprises
Comparison of Proposed Language for Regulation 1540
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Action Item *	Regulatory Language Proposed by Staff	Regulatory Language Proposed by Guild (Alternative 1)	Regulatory Language Proposed by Blonder (Alternative 2)	Regulatory Language Proposed by Wayne (Alternative 3)	Regulatory Language Proposed by Liao (Alternative 4)	Regulatory Language Proposed by AAAA (Alternative 5)
ACTION 6 - Definition of Intermediate Production Aids	(9) INTERMEDIATE PRODUCTION AIDS. Intermediate production aids include items such as artwork, illustrations, photograph images, photo engravings, and other similar materials which are used to produce special printing aids or other intermediate production aids. <i>[Interested parties have indicated concurrence with staff's proposed language for subdivision (a)(10) – see Exhibit 5, page 2.]</i>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	(9) INTERMEDIATE PRODUCTION AIDS. Intermediate production aids include items such as artwork, illustrations, photograph images, photo engravings, and other similar materials which are used to produce finished art or other intermediate production aids.	<i>[no comments received]</i>	(8) INTERMEDIATE PRODUCTION AIDS. Intermediate production aids include items such as artwork, clip-art (pre-packaged art) , illustrations, photograph images, photo engravings, and other similar materials which are used to produce special printing aids or other intermediate production aids.
ACTION 7 – Definition of Preliminary Art	(11) PRELIMINARY ART. Preliminary art is tangible personal property which is prepared solely for the purpose of demonstrating an idea or message for acceptance by the client before a contract is entered into or before approval is given for preparation of finished art to be furnished or licensed by the seller to his or her client, provided neither title to nor permanent possession of such tangible personal	<i>[same as staff's]</i>	<i>[same as staff's]</i>	(11) PRELIMINARY ART. Preliminary art is tangible personal property which is prepared solely for the purpose of demonstrating an idea or message for acceptance by the client before approval is given for preparation of finished art to be furnished or licensed by the seller to his or her client. The term “Preliminary art” implies that the same business entity that prepared the preliminary art,	<i>[no comments received]</i>	(10) PRELIMINARY ART. Preliminary art is tangible personal property which is prepared solely for the purpose of demonstrating an idea or message for acceptance by the client before a contract is entered into or before approval is given for preparation of finished art to be furnished or licensed by the seller to his or her client, provided neither title to nor permanent possession of such tangible personal property passes to the

* See comments for each action on pages 39-43. Action Items are not in strict numerical order on this schedule, since some Action Items reference numerous areas of the regulation.

Proposed Regulatory Changes Regarding Application of Tax to Graphic Arts and Related Enterprises
Comparison of Proposed Language for Regulation 1540
 Current as of January 16, 2002

Action Item *	Regulatory Language Proposed by Staff	Regulatory Language Proposed by Guild (Alternative 1)	Regulatory Language Proposed by Blonder (Alternative 2)	Regulatory Language Proposed by Wayne (Alternative 3)	Regulatory Language Proposed by Liao (Alternative 4)	Regulatory Language Proposed by AAAA (Alternative 5)
ACTION 3 – New Clarifying Language (Definition of Third Parties)	<p>property passes to the client. Preliminary art may include roughs, visualizations, layouts, comprehensives, and instant photos.</p> <p><i>[Interested parties have indicated concurrence with staff's proposed language for subdivision (a)(12) – see Exhibit 5, page 3.]</i></p>			<p>subsequently prepared finished art based on the approved preliminary art. Preliminary art may include roughs, visualizations, layouts, comprehensives, and instant photos.</p>		<p>client. Preliminary art consists of creative art services whose object is to convey ideas for review by the client and as such, any tangible personal property, is incidental to the true object of the transaction. Preliminary art may include, but is not limited to, roughs, visualizations, layouts, comprehensives, and instant photos. Preliminary art is not subject to tax.</p>
	<p><u>(13) THIRD PARTIES.</u> A reference in this regulation to a transfer to a client also includes a transfer to a third party on the client's behalf. For example, the discussion in subdivision (b)(2)(B) for transfers of finished art by loading into the client's computer also includes transfers of the finished art by loading it into a third party's computer at the instruction of the client.</p>	<p><i>[no comments received – staff added language after final interested parties submissions were received]</i></p>	<p><i>[no comments received – staff added language after final interested parties submissions were received]</i></p>	<p><i>[same as staff's]</i></p>	<p><i>[no comments received – staff added language after final interested parties submissions were received]</i></p>	<p><i>[no comments received – staff added language after final interested parties submissions were received]</i></p>

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Comparison of Proposed Language for Regulation 1540
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	<p>client title or the right to permanent possession of the artwork in tangible form, such as on electronic media or hard copy, or permanent possession of the artwork in tangible form is, in fact, transferred to the client.</p> <p>However, if the master agreement provides that the client owns the concepts embodied in</p>			<p>scope of the project is to provide consulting services only. The true intent of these services is to gain client approval to proceed with the preparation of finished art or, to provide nontaxable intangible consulting services. If the object of the job is to provide finished art and no approval is secured and no finished art was prepared, then these services are construed to be part of a "killed job" wherein no final product was produced and they are not taxable. Any tangible personal property produced is incidental to providing the service.</p> <p>However, if the master agreement provides that the client owns the concepts embodied in</p>		<p>incidental to the service provided and not subject to tax. However, if the master agreement provides that the advertising agency, artist or designer will pass to the client title or the right to permanent possession of the artwork in tangible form such as electronic media, or hard copy or permanent possession of the artwork in tangible form is in fact, transferred to the client, then tax is applicable. they are nontaxable unless the master agreement or other contract provides that the advertising agency or commercial artist will pass to the client title or the right to permanent possession of the artwork in tangible form, such as on electronic media or hard copy, or permanent possession of the artwork in tangible form is, in fact, transferred to the client</p> <p>However-If the contract master agreement provides that the client owns the concepts</p>

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	tangible personal property that is owned and possessed by the advertising agency or commercial artist (e.g., so that such concepts cannot be used on behalf of any other person), that contract provision does not constitute the passage of title to tangible personal property to the client, provided the client does not thereby obtain the actual title to, or permanent possession of, the tangible personal property embodying the concepts and no other contractual provision passes such title to, or permanent possession of, such tangible personal property. A requirement that an advertising agency or commercial artist retain permanent possession of the artwork in tangible form does not itself constitute a sale of that property to the client in the absence of a provision passing title to such property to the client.			tangible personal property that is owned and possessed by the advertising agency or commercial artist (e.g., so that such concepts cannot be used on behalf of any other person), that contract provision does not constitute the passage of title to tangible personal property to the client.		embodied in tangible personal property that is owned and possessed by the advertising agency or commercial artist (e.g., so that such concepts cannot be used on behalf of any other person), that contract master agreement provision does not constitute the passage of title to tangible personal property to the client, provided the client does not thereby obtain the actual title to, or permanent possession of, the tangible personal property embodying the concepts. A requirement that an advertising agency or commercial artist retain permanent possession of the artwork in tangible form does not itself constitute a sale of that property to the client. in the absence of a provision passing title to such property to the client.

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ACTION 8 – Application of Tax to Services – Passage of Title (continued)	<p>(b)(1)(A) 2. Tangible personal property developed and used during services performed to convey ideas, concepts, looks, or messages is consumed in the performance of those services. Unless, prior to any use, the advertising agency or commercial artist passes title to such property to the client as discussed in the previous paragraph,</p> <p>the advertising agency or commercial artist is the consumer of such tangible personal property used and tax applies to the sale of property to, or to the use of the property by, the advertising agency or commercial artist. If the advertising agency or commercial artist passes title to, or permanent possession of, such tangible personal property to its client, tax applies to the sale of the tangible personal property by the advertising agency or commercial artist to the client.</p>	<p>(b)(1)(A) <i>[same as staff's]</i></p>	<p>(b)(1)(A) <i>[same as staff's]</i></p>	<p>(b)(1)(A) 2. Tangible personal property developed and used during services performed to convey ideas, concepts, looks, or messages is consumed in the performance of those services. Unless, prior to any use, the advertising agency or commercial artist, acting as a retailer, passes title to such property to the client by means of a title clause in the contract of sale that passes title to the client prior to use, the advertising agency or commercial artist is the consumer of such tangible personal property used and tax applies to the sale of property to, or to the use of the property by, the advertising agency or commercial artist. If the advertising agency or commercial artist passes title to, or permanent possession of, such tangible personal property to its client, tax applies to the sale of the tangible personal property by the advertising agency or commercial artist to the client.</p>	<p>(b)(1)(A) <i>[no comments received]</i></p>	<p>(c)(1)(A) <i>[same as staff's]</i></p>

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ACTION 3 – New Clarifying Language (Digital Pre- Press Instruction)	(b)(1) (B) Digital Pre-Press Instruction. <u>Digital pre-press instruction is a custom computer program under section 6010.9 of the Revenue and Taxation Code, the sale of which is not subject to tax, provided the digital pre-press instruction is prepared to the special order of the purchaser.</u>	(b)(1) <i>[no comments received – staff added language after final interested parties submissions were received]</i>	(b)(1) <i>[no comments received – staff added language after final interested parties submissions were received]</i>	(b)(1) <i>[no comments received – staff added language after final interested parties submissions were received]</i>	(b)(1) <i>[no comments received – staff added language after final interested parties submissions were received]</i>	(c)(1) (B) Digital Pre-Press Instruction. A file prepared to the special order of the client which qualifies as digital pre-press instruction as defined in subdivision (f) of Regulation 1541 is a custom computer program, and its transfer is not subject to tax regardless of the form in which the file is transferred or the time at which it is transferred.
ACTION 21 – General Language Differences [Alternative 5]	<u>Digital pre-press instruction shall not, however, be regarded as a custom computer program if it is a “canned” or prewritten computer program which is held or existing for general or repeated sale or lease, even if the digital pre-press instruction was initially developed on a custom basis or for in-house use. The sale of such canned or prewritten digital pre-press instruction in tangible form is a sale of tangible personal property, the retail sale of which is subject to tax.</u>					Electronic or digital pre-press instruction shall not, however, be regarded as a custom computer program if it is a “canned” or prewritten computer program which is held or existing for general or repeated sale or lease, even if the electronic or digital pre-press instruction was initially developed on a custom basis or for in-house use. In such cases, the “canned” software is taxable.

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ACTION 21 – General Language Differences [Alternative 5] ACTION 9 – Specific Nontaxable charges [Alternative 3]	<i>[Interested parties have indicated concurrence with staff's proposed language for subdivision (b)(1)(C) through (b)(1)(E)– see Exhibit 5, page 4.]</i> (b)(1) (F) Specific Nontaxable Charges. The following and similar fees and commissions are not taxable when they are separately stated. Whether separately stated or not, these fees and commissions are not included in the calculation of “direct labor” for purposes of subdivision (b)(3).	(b)(1) <i>[same as staff's]</i>	(b)(1) <i>[same as staff's]</i>	(b)(1) (F) Specific Nontaxable Charges. The following and similar fees and commissions are not taxable when they are separately stated. Whether separately stated or not, these fees and commissions are considered to be markup for purposes of subdivision (b)(3). (1) Agent fees added to purchases of tangible personal property by agencies established as agents for their clients as compensation for their performances of services related to such purchases	(b)(1) <i>[no comments received]</i>	(c)(1) (F) Specific Nontaxable Charges. The following , and similar fees and commissions are not taxable when they are separately stated. Whether separately stated or not, these fees and commissions are not included in the calculation of “direct labor” for purposes of subdivision (b)(3).
	(b)(1)(F) 1. Media commissions received for placement of	<i>[same as staff's]</i>	<i>[same as staff's]</i>	(b)(1)(F) <i>[Subsequent commissions and fees would be</i>	<i>[no comments received]</i>	(c)(1)(F) 1. Media commissions or fees received for

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	advertising whether paid by the medium, by another advertising agency, or by the client. 2. Commissions paid to advertising agencies by suppliers. Examples of such commissions are those paid to an advertising agency by a premium manufacturer (or distributor) or a direct-by-mail supplier. <i>[Interested parties have indicated concurrence with staff's proposed language for subdivision (b)(1)(F)3. through (F)6. – see Exhibit 5, page 5.]</i>			<i>renumbered 2 through 7 - otherwise same as staff's]</i>		placement of advertising whether paid by the medium, by another advertising agency, or by the client. 2. Commissions or fees paid to advertising agencies by suppliers. Examples of such commissions are those paid to an advertising agency by a premium manufacturer (or distributor) or a direct-by-mail supplier.
ACTION 3 - New Clarifying Language (Example for Application of Tax)	(b)(1) _____(G) Example. <u>A designer contracts to create and sell printed brochures to a law firm. The contract separately states a charge for design, for art direction, for preliminary art, and for the printed brochures. The designer's design and art direction services culminate in the creation of preliminary art that the designer uses to show the</u>	<i>[same as staff's]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>

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	<p><u>designer's concepts to the law firm. After the law firm approves the concepts, the designer finalizes the design of the brochure and contracts with a printer to print the brochures. The printer sells the printed brochures to the designer for resale, and the designer resells the printed brochures to the law firm. The only tangible personal property that will be transferred to the law firm (or to anyone on behalf of the law firm) are the printed brochures. The law firm will not obtain title to, or the right to possession of, any finished art or any other tangible personal property. Tax does not apply to the designer's separately stated charges for design, art direction, and preliminary art. Tax applies to the designer's separately stated charge to the law firm for the printed brochures.</u></p> <p><i>[Interested parties have indicated concurrence with staff's proposed language for subdivision (b)(2)(A) – see Exhibit 5, page 5.]</i></p>					

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ACTION 10 – Use of Aids in Creation of Finished Art – Title Clause Agreement	<p><u>(b)(2) FINISHED ART.</u></p> <p>(A) Use of Aids in Creation of Finished Art.</p> <p>No subdivision recommended.</p>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<p>(c)(2) FINISHED ART.</p> <p>(A) Use of Aids in Creation of Finished Art.</p> <p>(1) Prior to the preparation of finished art, if the client signs a title clause agreement to purchase intermediate production aids or obtain the lease rights for illustrations, electronic art, photography, typography, airbrushing, photo retouching, filmwork, photostats, dies, lithographic film and plates, photo engravings, and other materials needed to prepare the finished artwork, the intermediate production aids are taxed only once.</p>
ACTION 21– General Language Differences	<p>(b)(2) (B) Transfers of Finished Art Not in Tangible Form.</p> <p>A transfer of electronic artwork from an advertising agency or commercial artist to the client or to a third party</p>	<p>(b)(2) <i>[same as staff's]</i></p>	<p>(b)(2) <i>[same as staff's]</i></p>	<p>(b)(2) <i>[same as staff's]</i></p>	<p>(b)(2) <i>[no comments received]</i></p>	<p>(c)(2) (B) Transfers of Finished Art Not in Tangible Form. (Electronic Artwork). A transfer of electronic artwork from an advertising agency or commercial artist to the client or to a third party</p>

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	on the client's behalf that is not in tangible form is not a sale of tangible personal property, and the charges for the transfer are not subject to tax. A transfer of electronic artwork is not in tangible form if the file containing the electronic artwork is transferred through remote telecommunications (such as by modem or over the Internet), or if the file is loaded into the client's computer by the advertising agency or commercial artist, and the client does not obtain title to or possession of any tangible personal property, such as electronic media or hard copy. If the transfer is not a transfer in tangible form because it is loaded onto the client's computer, the advertising agency or commercial artist should document that transfer by a written statement signed at the time of loading by the client and by the person who loaded the electronic artwork into the client's computer with the following or similar language: "This electronic					on the client's behalf that is not in tangible form is not a sale of tangible personal property, and the charges for the transfer are not subject to tax. A transfer of electronic artwork is not in tangible form if the file containing the electronic artwork is transferred through remote telecommunications (such as by modem or over the Internet), or if the file is loaded into the client's computer by the advertising agency or commercial artist, and the client does not obtain title to or possession of any tangible personal property, such as electronic media or hard copy. If the transfer is not a transfer in tangible form because it is loaded onto the client's computer, the advertising agency or commercial artist should document that transfer by a written statement signed at the time of loading by the client and by the person who loaded the electronic artwork into the client's computer with the following or similar language: "This electronic

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ACTION 21 – General Language Differences	<p>artwork was loaded into the computer of [client's name] by [seller's name], and [seller's name] did not transfer any tangible personal property containing the artwork, such as electronic media or hard copies, to [client's name].”</p> <p>When such a statement is signed at the time the file is loaded,</p> <p>it will be rebuttably presumed that the transfer of electronic artwork was not transferred in tangible form. If there is no such timely completed statement, the advertising agency or commercial artist may provide other substantive evidence establishing that the artwork was not transferred in tangible form.</p> <p>(b)(2) (C) Transfers of Finished Art in Tangible Form. The electronic or manual preparation of</p>	<p>(b)(2) <i>[same as staff's]</i></p>	<p>(b)(2) <i>[same as staff's]</i></p>	<p>(b)(2) (C) Transfers of Finished Art in Tangible Form. The electronic or manual preparation of</p>	<p>(b)(2) <i>[no comments received]</i></p>	<p>artwork was loaded into the computer of [client's name] by [advertising agency, artist or designer's name] and [advertising agency, artist or designer's name] did not transfer any tangible personal property containing the artwork, such as electronic media or hard copies, to [client's name].” When such a statement is signed or initialed at the time the file is loaded or at the point the transfer is invoiced to the client, it will be rebuttably presumed that the transfer of electronic artwork was not transferred in tangible form. If there is no such timely completed statement, the advertising agency or commercial artist may provide other substantive evidence establishing that the artwork was not transferred in tangible form.</p> <p>(c)(2) (C) Transfers of Finished Art in Tangible Form. The electronic or manual preparation of</p>

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ACTION 21 – General Language Differences ACTION 2 – Organization of Regulation [Created subdivision (b)(2)(C)1.]	finished art for use in reproduction or display is not a service. Unless the transfer is not in tangible form as explained in subdivision (b)(2)(B), the transfer of finished art is a sale of tangible personal property and tax applies to charges for that finished art, including all charges for any rights sold with the finished art, such as copyrights or distribution and production rights, except as provided in subdivision (b)(2)(D)2. If charges for finished art are combined into a single charge that also includes nontaxable charges for conceptual services described in subdivision (b)(1)(A), the advertising agency or commercial artist may report the measure of tax on the retail sale of the finished art as specified in subdivision (b)(3), provided that the reported measure of tax must also include the value of reproduction rights included with the transfer except those that are not taxable as provided in subdivision (b)(2)(D)2.			finished art for use in reproduction or display is not a service. Unless the transfer is not in tangible form as explained in subdivision (b)(2)(B), the transfer of finished art is a sale of tangible personal property and tax applies to charges for that finished art, including all charges for any rights sold with the finished art, such as copyrights or distribution and production rights, except as provided in subdivision (b)(2)(D)2. If charges for finished art are combined into a single charge that also includes nontaxable charges for conceptual services described in subdivision (b)(1)(A), the advertising agency or commercial artist may report the measure of tax on the retail sale of the finished art as specified in subdivision (b)(3), provided that the reported measure of tax must also include the value of reproduction rights included with the transfer except those that are not taxable as provided in subdivision (b)(2)(D)2.		finished art for use in reproduction or display is not a service. Unless the transfer is not in tangible form as explained in subdivision (b)(2)(B), The transfer of finished art in tangible form is a sale of tangible personal property and tax applies to charges for that finished art, including all charges for any rights sold with the finished art such as copyrights or distribution and production rights, except as provided in subdivision (b)(2)(D)2. If charges for finished art are combined into a single charge that also includes nontaxable charges for conceptual services described in subdivision (b)(1)(A), the advertising agency or commercial artist may report the measure of tax on the retail sale of the finished art as specified in subdivision (b)(3), provided that the reported measure of tax must also include the value of reproduction rights included with the transfer except those that are not taxable as provided in subdivision (b)(2)(D)2.

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	<p>If tax is not reported on this basis, it will be rebuttably presumed that 75 percent of the combined charge for the finished art and conceptual services is for the nontaxable services and that 25 percent of the combined charge is the measure of tax on the retail sale of the finished art, provided that 25 percent of the combined charge is not less than the sales price to the advertising agency or commercial artist of the finished art (or component parts) and any intermediate production aids or special printing aids sold to the client for that combined charge.</p>			<p>If tax is not reported on this basis, it will be rebuttably presumed that 75 percent of the combined charge for the finished art and conceptual services is for the nontaxable services and that 25 percent of the combined charge is the measure of tax on the retail sale of the finished art, provided that 25 percent of the combined charge is not less than the sales price to the advertising agency or commercial artist of the finished art (or component parts) and any intermediate production aids or special printing aids sold to the client for that combined charge.</p>		<p>1. Lump sum billing of in-house artwork containing preliminary art and finished art.</p> <p>An advertising agency, artist or designer may elect to do a lump-sum billing of in-house artwork containing both preliminary art and finished art. If tax is not reported on this basis, On billing of in-house artwork for which an advertising agency, artist or designer makes a lump-sum charge that includes both preliminary art and other nontaxable services and finished art, it will be rebuttably presumed that 75 percent of the combined charge for the finished art and conceptual services is for the nontaxable services and that 25 percent of the combined charge is the measure of tax on the retail sale of the finished art, provided that 25 percent of the combined charge is not less than the sales price to the advertising agency or commercial artist of the finished art (or</p>

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ACTION 11 – Transfers of Finished Art in Tangible Form – Cost of Special Printing Aids	If such sales price to the advertising agency or commercial artist is more than 25 percent of the combined charge to the client, the measure of tax shall be deemed to be such sales price of the tangible personal property to the advertising agency or commercial artist.	<i>[same as staff's]</i>	<i>[same as staff's]</i>	If such sales price to the advertising agency or commercial artist is more than 25 percent of the combined charge to the client, the measure of tax shall be deemed to be such sales price of the tangible personal property to the advertising agency or commercial artist.	<i>[no comments received in response to staff's revised language]</i>	component parts) and any intermediate production aids or special printing aids sold to the client for that combined charge. If such sales price to the advertising agency or commercial artist is more than 25 percent of the combined charge to the client, the measure of tax shall be deemed to be such sales price of the tangible personal property to the advertising agency or commercial artist.
ACTION 12 – Transfers of Finished Art in Tangible Form – Option to Separately State Special Printing Aids				Intermediate production aids or special printing aids sold to the client that are separately listed and priced on the invoice to the client are subject to the rules governing an advertising agency acting as an agent or retailer as described in subdivision (c).		
ACTION 13 – Technology Transfer Agreement – Requirement That It Be in Writing	(b)(2) (D) Reproduction Rights Transferred With Finished Art. 2. Any agreement evidenced by a writing (such as a contract, invoice, or purchase	(b)(2) (D) Reproduction Rights Transferred With Finished Art. 2. Any agreement evidenced by a writing (such as a contract, invoice, or purchase	(b)(2) <i>[same as staff's]</i>	(b)(2) <i>[same as staff's]</i>	(b)(2) (D) Reproduction Rights Transferred With Finished Art. 2. Any agreement that assigns or licenses a copyright interest in finished art for the	(c)(2) <i>[same as staff's]</i>

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ACTION 14 – Technology Transfer Agreement - Finished Art Transferred on Computer Storage Media	order) that assigns or licenses a copyright interest in finished art for the purpose of reproducing and selling other property subject to the copyright interest is a technology transfer agreement, as explained further in Regulation 1507. Tax applies to amounts received for any tangible personal property transferred as part of a technology transfer agreement.	order) that assigns or licenses a copyright interest in finished art for the purpose of reproducing and selling other property subject to the copyright interest is a technology transfer agreement, as explained further in Regulation 1507. Tax applies to amounts received for any tangible personal property transferred as part of a technology transfer agreement. Notwithstanding subdivision (b)(2)(B), tax does not apply to temporary transfers of computer storage media containing finished art transferred as part of a technology transfer agreement.			purpose of reproducing and selling other property subject to the copyright interest is a technology transfer agreement, as explained further in Regulation 1507. Tax applies to amounts received for any tangible personal property transferred as part of a technology transfer agreement.	
	Tax does not apply to amounts received for the assignment or licensing of a copyright interest as part of a technology transfer agreement. The measure of tax on the sale of finished art transferred by an advertising agency or commercial artist as part of a technology transfer agreement shall be:	Tax does not apply to amounts received for the assignment of a copyright interest to a third party as part of a technology transfer agreement. The measure of tax on the sale of finished art transferred by an advertising agency or commercial artist as part of a technology transfer agreement shall be:			Tax does not apply to amounts received for the assignment or licensing of a copyright interest as part of a technology transfer agreement. The measure of tax on the sale of finished art transferred by an advertising agency or commercial artist as part of a technology transfer agreement shall be:	

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ACTION 21 – General Language Differences [Alternative 2] ACTION 15 Technology Transfer Agreement – Separately Stated Price	(b)(2)(D)2 a. The separately stated sales price for the finished art, provided the separately stated price represents a fair market value of the tangible personal property;	(b)(2)(D)2 a. The separately stated sales price for the finished art, provided the separately stated price is reasonable ;	(b)(2)(D)2 a. The separately stated sales price for the finished art, provided the separately stated price represents either (i) the fair market value of the tangible personal property; or (ii) if the possession of the finished art is transferred temporarily for purposes of reproduction, the fair rental value of the tangible personal property ;	(b)(2)(D)2 a. <i>[same as staff's]</i>	(b)(2)(D)2 a. <i>[same as staff's]</i>	(c)(2)(D)2 a. <i>[same as staff's]</i>
	ACTION 3 - New Clarifying Language (Finished Art and Like Finished Art) b. Where there is no such separately stated price, the separate price at which the person holding the copyright interest in the finished art has sold or leased <u>that finished art or</u> <u>like finished art to an</u> <u>unrelated third party</u> <u>where: 1) the finished art</u> <u>was sold or leased</u> <u>without also transferring</u> <u>an interest in the</u> <u>copyright; or 2) the</u> <u>finished art was sold or</u> <u>leased in another</u> <u>transaction at a stated</u> <u>price satisfying the</u> <u>requirements of</u> <u>subdivisions</u> (b)(2)(D)2.a.; or	<i>[same as staff's]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>

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Proposed Regulatory Changes Regarding Application of Tax to Graphic Arts and Related Enterprises
Comparison of Proposed Language for Regulation 1540
 Current as of January 16, 2002

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ACTION 17 – Cost of Materials – Includes Those Used as Well as Incorporated [Alternative 4]	c. If there is no such separately stated price under subdivision (b)(2)(D)2.a., nor a separate price under subdivision (b)(2)(D)2.b., 200 percent of the combined cost of materials and labor used to produce or acquire the finished art. “Cost of materials” consists of the costs of those materials used or incorporated into the finished art, or any tangible personal property transferred as part of the technology transfer agreement. “Labor” includes any charges or value of labor used to create such tangible personal property whether the advertising agency or commercial artist performs such labor, a third party performs the labor, or the labor is performed through some combination thereof. The value of labor provided by the advertising agency or commercial artist shall equal the lower of the normal and customary charges for labor billed to third parties by the advertising agency or	c. If there is no such separately stated price under subdivision (b)(2)(D)2.a., nor a separate price under subdivision (b)(2)(D)2.b., 200 percent of the combined cost of materials and labor used to produce or acquire the finished art. “Cost of materials” consists of the costs of those materials used or incorporated into the finished art, or any tangible personal property transferred as part of the technology transfer agreement. “Labor” means any charges for labor used to create such tangible personal property where the advertising agency or commercial artist purchases such labor from a third party or the work is performed by an employee of the advertising agency or commercial artist.	c. If there is no such separately stated price under subdivision (b)(2)(D)2.a., nor a separate price under subdivision (b)(2)(D)2.b., 200 percent of the combined cost of materials and labor used to produce or acquire the finished art. “Cost of materials” consists of the costs of those materials used or incorporated into the finished art, or any tangible personal property transferred as part of the technology transfer agreement. “Cost of labor” includes any consideration paid to an employee or an independent contractor for labor used to create such tangible personal property.	[same as staff’s]	c. If there is no such separately stated price under subdivision (b)(2)(D)2.a., nor a separate price under subdivision (b)(2)(D)2.b., 200 percent of the combined cost of materials and labor used to produce or acquire the finished art. “Cost of materials” consists of the costs of those materials physically incorporated into the finished art, or any tangible personal property transferred as part of the technology transfer agreement. “Labor” includes any charges or value of labor used to create such tangible personal property whether the advertising agency or commercial artist performs such labor, a third party performs the labor, or the labor is performed through some combination thereof. The value of labor provided by the advertising agency or commercial artist shall equal the lower of the normal and customary charges for labor billed to third parties by the advertising agency or	c. If there is no such separately stated price under subdivision (b)(2)(D)2.a., nor a separate price under subdivision (b)(2)(D)2.b., 200 percent of the combined cost of materials and labor used to produce or acquire the finished art. “Cost of materials” consists of the costs of those materials used or incorporated into the finished art, or any tangible personal property transferred as part of the technology transfer agreement. “Labor” includes any charges or value of labor used to create such tangible personal property whether the advertising agency or commercial artist performs such labor, a third party performs the labor, or the labor is performed through some combination thereof. The value of labor provided by the advertising agency or commercial artist shall equal the lower of the normal and customary charges for labor billed to third parties by the advertising agency or
ACTION 16 – Technology Transfer Agreement – the Value of the Artist’s Labor [Alternative 1 and 2]						

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ACTION 21 – General Language Differences [Alternative 5] ACTION 16 – Technology Transfer Agreement – the Value of the Artist’s Labor (continued)	commercial artist, or the fair market value of the labor performed by the advertising agency or commercial artist.	<i>[If staff’s recommendation is adopted, the Guild proposes the following language be added as the last sentence of the paragraph.]</i> In the absence of evidence of a price charged by that commercial artist or advertising agency for labor only, the fair market value for such labor shall be presumed to be \$100.			commercial artist, or the fair market value of the labor performed by the advertising agency or commercial artist.	commercial artist, or the fair market value of the labor performed by the advertising agency or commercial artist. Nontaxable fees, charges and commissions are not included in the calculation of direct labor (see (c) (1) (f)).
	ACTION 18 – Explanation of Calculation of Sales Price of Other Tangible Personal Property	(b)(3) <i>[same as staff’s]</i>	(b)(3) <i>[same as staff’s]</i>	(b)(3) <i>[same as staff’s]</i>	(b)(3) <i>[no comments received]</i>	(b)(3) SALES OF OTHER TANGIBLE PERSONAL PROPERTY BY ADVERTISING AGENCY OR COMMERCIAL ARTIST. Tax applies to the total charge for the retail sale of tangible personal property by an advertising agency or commercial artist. If an advertising agency or commercial artist combines charges for nontaxable services as defined in subdivision

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	(b)(1)(F), such as media placement, with charges for tangible personal property for which the advertising agency or commercial artist is the retailer, the measure of tax on that retail sale of property includes the total of: direct labor; the cost of purchased items that become an ingredient or component part of the tangible personal property; the cost of any intermediate production aids or special printing aids; and a reasonable markup. Commissions, fees, and other charges exclusively related to the production or fabrication of tangible personal property are part of direct labor and are thus included in the measure of tax. Such charges include retouching of photographic images or other artwork for reproduction, provided the retouching is intended to improve the quality of the reproduction. An advertising agency or commercial artist must keep sufficient records to document the basis for the reported measure of tax.					(b)(1)(F), such as media placement, with charges for tangible personal property for which the advertising agency or commercial artist is the retailer, the measure of tax on that retail sale of property includes the total of: direct labor; the cost of purchased items that become an ingredient or component part of the tangible personal property; the cost of any intermediate production aids or special printing aids; and a reasonable markup. Commissions, fees, and other charges exclusively related to the production or fabrication of tangible personal property are part of direct labor and are thus included in the measure of tax. Such charges include retouching of photographic images or other artwork for reproduction, provided the retouching is intended to improve the quality of the reproduction. An advertising agency or commercial artist must keep sufficient records to document the basis for the reported measure of tax.

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ACTION 21 – General Language Differences	(b)(4) ITEMS PURCHASED BY AN ADVERTISING AGENCY OR COMMERCIAL ARTIST. Except when property is resold prior to any use, an advertising agency or commercial artist is the consumer of tangible personal property used in the operation of its business. Tax applies to the sale of such property to, or to the use of such property by, the advertising agency or commercial artist.	(b)(4) <i>[same as staff's]</i>	(b)(4) <i>[same as staff's]</i>	(b)(4) <i>[same as staff's]</i>	(b)(4) <i>[no comments received]</i>	(b)(4) ITEMS PURCHASED BY AN ADVERTISING AGENCY OR COMMERCIAL ARTIST. Except when property is resold prior to any use, an advertising agency or commercial artist is the consumer of tangible personal property used in the operation of its business. Tax applies to the sale of such property to, or to the use of such property by, the advertising agency or commercial artist.
	(c) SITUATIONS SPECIFIC TO ADVERTISING AGENCIES. (1) ADVERTISING AGENCY ACTING AS AN AGENT FOR ITS CLIENT. An agent is one who represents another, called the principal, in dealings with third persons. (Civil Code section 2295.) To the extent that an advertising agency acts as the agent of its client when acquiring tangible personal property, it is	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[no comments received]</i>	(b) SITUATIONS SPECIFIC TO ADVERTISING AGENCIES. (1) ADVERTISING AGENCY ACTING AS AN AGENT FOR ITS CLIENT. An agent is one who represents another, called the principal, in dealings with third persons. (Civil Code section 2295). To the extent that an advertising agency acts as the agent of its client when acquiring tangible personal property, it is

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ACTION 21 – General Language Differences	neither a purchaser of the property with respect to the supplier nor a seller of the property with respect to its principal (that is, its client). Because of the unique relationship between advertising agencies and their clients, unless an advertising agency elects non-agent status under subdivision (c)(2)(A) or is otherwise the retailer of the property under subdivision (c)(2)(B) or (c)(2)(C), it is rebuttably presumed that the advertising agency acts as the agent of its client when acquiring tangible personal property on its client's behalf.					neither a purchaser of the property with respect to the supplier nor a seller of the property with respect to its principal (that is, its client). Because of the unique relationship between advertising agencies and their clients, unless the advertising agency elects non-agent status under subdivision (c)(2)(A), or is otherwise the retailer of the property under subdivision (c)(2)(B) or (c)(2)(C) it is rebuttably presumed that the advertising agency acts as an agent of its client when acquiring tangible personal property on its client's behalf. (See (c)(2)(A),(B),(C).
	(c)(1) (A) A supplier of tangible personal property to an advertising agency is presumed to have made a retail sale of that property unless the supplier takes a timely and valid resale certificate in good faith from the advertising agency. Otherwise, the supplier has the burden of establishing that the advertising agency	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[no comments received]</i>	(b)(1) (A) A supplier of tangible personal property to an advertising agency is presumed to have-made a retail sale of that property unless the supplier takes a timely and valid resale certificate in good faith from the advertising agency. Otherwise, the supplier has the burden of establishing that the advertising agency

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ACTION 21 – General Language Differences	<p>elected non-agent status under subdivision (c)(2)(A) and resold the property or that the advertising agency resold the property as the retailer under subdivision (c)(2)(B) or (c)(2)(C).</p> <p>(c)(1) <i>[Interested parties have indicated concurrence with staff's proposed language for subdivision (c)(1)(B) – see Exhibit 5, page 8.]</i></p>					<p>elected non-agent status under subdivision (c)(2)(A) and resold the property or that the advertising agency resold the property as the retailer under subdivision (c)(2)(B) or (c)(2)(C).</p>
ACTION 19 – Evidence to Prove Erroneous Issuance of a Resale Certificate	<p>(c)(1) (C) An advertising agency may not issue a resale certificate when purchasing tangible personal property as the agent of its client. An advertising agency who issues a resale certificate to a supplier is presumed to be purchasing tangible personal property from that supplier on its own behalf for resale and not to be acting as an agent of its client. However, the advertising agency may provide evidence to prove that its issuance of the resale certificate was erroneous and that the advertising agency was</p>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[no comments received]</i>	<p>(b)(1) (C) An advertising agency may not issue a resale certificate when purchasing tangible personal property as the agent of its client. An advertising agency who issues a resale certificate to a supplier is presumed to be purchasing tangible personal property from that supplier on its own behalf for resale and is not to be acting as an agent of its client. However, the advertising agency may provide evidence to prove that its issuance of the resale certificate was erroneous and that the advertising</p>

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ACTION 19 – Evidence to Prove Erroneous Issuance of a Resale Certificate (continued)	acting as an agent of its client, provided the advertising agency has not treated the transaction as its own sale of tangible personal property to its client, collecting tax or tax reimbursement from its client on that sale. If the resale certificate was issued in error, the advertising agency is liable for use tax on the cost of tangible personal property purchased under the certificate unless the advertising agency has already paid that tax to the supplier or to the Board, or the client has self-reported and paid the tax to the Board.					agency was acting as an agent of its client; provided the advertising agency has not treated the transactions as its own sale of tangible personal property or its client, collecting tax or tax reimbursement from its client on that sale. If the resale certificate was issued in error, the advertising agency is liable for use tax on the cost of tangible personal property purchased under the certificate unless the advertising agency has already paid that tax to the supplier or to the Board, or the client has self-reported and paid the tax to the Board.
ACTION 3 - New Clarifying Language (Advertising Agency Acting as Retailer)	(c)(2) ADVERTISING AGENCY ACTING AS A RETAILER. An advertising agency that acts as a retailer of tangible personal property may issue a resale certificate for such tangible personal property if the property will be resold prior to any use. <u>Absent an agreement that the property will be sold prior to use, tax is due on the purchase price of</u>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[same as staff's]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>

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	<p><u>tangible personal property that is used prior to being resold to the client and, in addition, tax is also due on the sales price of the tangible personal property to the client.</u></p> <p>(A) Election of Non-Agent Status. An advertising agency may elect non-agent status with respect to sales of tangible personal property to its client. This election must be supported by a specific written statement in its master agreement with the client. Alternatively, a statement may be included on an advertising agency's job order or invoice to its client. Statements should include the following or similar language: "(Advertising Agency's name) will not be acting as an agent of (client's name) for purposes of this transaction."</p> <p>An advertising agency that elects non-agent status is a retailer with respect to tangible personal property sold to its clients. The measure of tax on the advertising</p>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[no comments received]</i>	<p>(A) Election of Non-Agent Status. An advertising agency may elect non-agent status with respect to sales of tangible personal property to its client. This election must be supported by a specific written statement in its master agreement with the client. Alternatively, a statement may be included on an advertising agency's job order or invoice to its client. Statements should include the following or similar language: "(Advertising Agency's name) will not be acting as an agent of (client's name) for purposes of this transaction."</p> <p>An advertising agency that elects non-agent status is a retailer with respect to tangible personal property sold to its clients. The measure of tax on the advertising</p>

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ACTION 21 – General Language Differences	agency's retail sale is the separately stated charge for the tangible personal property. If there is no such separately stated charge, the measure of tax is calculated as provided in subdivision (b).					agency's retail sale is the separately stated charge for the tangible personal property. If there is no such separately stated charge, the measure of tax is calculated as provided in subdivision (c).
	(c)(2) (B) Items Produced or Fabricated by an Advertising Agency in-House. Advertising agencies are retailers of tangible personal property they produce or fabricate, e.g., by their own employees. Advertising agencies are not agents of their clients with respect to the acquisition of materials incorporated into such items of tangible personal property they produce or fabricate,	(c)(2) <i>[same as staff's]</i>	(c)(2) <i>[same as staff's]</i>	(c)(2) (B) Items Produced or Fabricated by an Advertising Agency in-House. Advertising agencies are retailers of tangible personal property they produce or fabricate, e.g., by their own employees. Advertising agencies are not agents of their clients with respect to the acquisition of materials incorporated into such items of tangible personal property they produce or fabricate,	(c)(2) <i>[no comments received]</i>	Except for in-house artwork billed on a lump sum method under section (c)(5), tax is due on the taxable selling price of tangible personal property . If there is no separately stated charge, the taxable selling price may be calculated as shown in subdivision (c). (b)(2) (B) Items Produced or Fabricated by an Advertising Agency in-House. Advertising agencies are retailers of tangible personal property they produce or fabricate, e.g., by their own employees. Advertising agencies are not agents of their clients with respect to the acquisition of materials incorporated into such items of tangible personal property they produce or fabricate,

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ACTION 21 – General Language Differences [Alternative 3 and 5]	but instead are the retailers of such property. The measure of tax on their retail sale of that property is the separately stated charge for the property sold. If there is no such separately stated charge, the measure of tax is calculated as provided in subdivision (b).			but instead are the retailers of such property. The measure of tax on their retail sale of that property is the separately stated charge for the property sold. If there is no such separately stated charge, the measure of tax is calculated as provided in subdivision (b). The term “incorporated” means those items that become an ingredient or part of the property and not those that are merely consumed or used in the production of the property sold. For example, materials such as bronze in a sculpture or canvas in a painting are incorporated into the property and may not be treated as an agent transaction. A photograph is not incorporated into finished art if only a copy of the photograph was incorporated into the finished art and it may be treated as an agent transaction. (c)(1).		but instead are the retailers of such property. The measure of tax on their retail sale of that property is the separately stated charge for the property sold. If there is no such separately stated charge, the measure of tax is calculated as provided in subdivision (c). Except for in-house artwork billed as a lump-sum under section (c)(5), tax is due on the taxable selling price of tangible personal property fabricated or produced by the advertising agency's employees. In those situations, an advertising agency should issue a resale certificate when purchasing items that become part of such tangible personal property.

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ACTION 20 – Invoice to Client for More Than Cost of Property	(c)(2) (C) Invoice to Client for More Than Cost of Tangible Personal Property to Advertising Agency. When an advertising agency invoices its client for tangible personal property provided by the advertising agency without separately stating the amount paid to the supplier for that property, the advertising agency is the retailer of the tangible personal property to its client. For example, when the advertising agency invoices a single charge to its client for tangible personal property that includes the amount paid to the supplier for the tangible personal property together with a markup, the advertising agency is the retailer of that tangible personal property and tax applies to that separately stated charge. If the advertising agency makes a lump sum charge to its client that includes the charge for the tangible personal property as well as the charge for any nontaxable services or reproduction rights under	(c)(2) <i>[same as staff's]</i>	(c)(2) <i>[same as staff's]</i>	(c)(2) <i>[same as staff's]</i>	(c)(2) <i>[no comments received]</i>	(b)(2) —(C) Invoice to Client for More Than Cost of Tangible Personal Property to Advertising Agency. When an advertising agency invoices its client for tangible personal property provided by the advertising agency without separately stating the amount paid to the supplier for that property, the advertising agency is the retailer of the tangible personal property to its client. For example, when the advertising agency invoices a single charge to its client for tangible personal property that includes the amount paid to the supplier for the tangible personal property together with a markup, the advertising agency is the retailer of that tangible personal property and tax applies to that separately stated charge. If the advertising agency makes a lump sum charge to its client that includes the charge for the tangible personal property as well as the charge for any nontaxable services or reproduction rights under

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ACTION 3 – New Clarifying Language (Printed Sales Messages)	subdivision (b), the advertising agency is the retailer of the tangible personal property provided and the measure of tax on the sale of that tangible personal property is calculated as provided in subdivision (b). <i>[Interested parties have indicated concurrence with staff's proposed language for subdivision (d)– see Exhibit 5, page 10.</i>					subdivision (b), the advertising agency is the retailer of the tangible personal property provided and the measure of tax on the sale of that tangible personal property is calculated as provided in subdivision (b).
	(e) CHARGES AND TRANSACTIONS GOVERNED BY OTHER REGULATIONS. <i>[Interested parties have indicated concurrence with staff's proposed language for subdivisions (e)(1), (e)(2), and (e)(4) – see Exhibit 5, page 10.</i>					(e) CHARGES AND TRANSACTIONS GOVERNED BY OTHER REGULATIONS.
	(3) PRINTED SALES MESSAGES. Qualifying sales of printed sales messages may qualify for exemption, as explained in Regulation 1541.5.	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[same as staff's]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>	<i>[no comments received – staff added language after final interested parties submissions were received]</i>

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ACTION 21 – General Language Differences	(5) VIDEO OR FILM PRODUCTIONS. When a video or film production obtained or furnished by an advertising agency to its client constitutes qualified production services as defined in Regulation 1529, tax applies to the charges for such qualified production services as provided in Regulation 1529.	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	<i>[same as staff's]</i>	(4) VIDEO OR FILM PRODUCTIONS. When a video or film production obtained or furnished by an advertising agency to its client constitutes qualified production services as defined in Regulation 1529, tax does not apply applies to the charges for such qualified production services as provided in Regulation 1529. Similarly, tax does not apply to charges for creative art services or for qualified production services.

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SUMMARY COMMENTS

ACTION 2 – Organization of Regulation – (b) and (c)

Throughout: AAAA combined staff's suggested format with the revised format from the second discussion paper. The primary difference is the reversal of subdivisions (b) and (c). Staff's proposed format is consistent with other regulations and flows more smoothly. Other interested parties agree with staff's format.

ACTION 3 – New Clarifying Language Proposed by Staff

Staff provided revised language to interested parties on 12-19-01. After receiving responses from interested parties, staff made the following revisions based on those suggestions.

Page 5 - **(a)(5)**: Incorporated the definition of digital pre-press instruction from Regulation 1541.

Page 9 – **(a)(13)**: Incorporated a definition for third parties.

Page 14 - **(b)(1)(B)**: Incorporated language to clarify the application of tax to sales of digital pre-press instruction.

Page 16 – **(b)(1)(G)**: Incorporated an example to demonstrate the application of tax to advertising agencies and commercial artists.

Page 25 – **(b)(2)(D)2.b.**: Incorporated language regarding "like finished art."

Page 32 – **(c)(2)**: Incorporated language regarding the application of tax to an advertising agency acting as a retailer.

Page 37 – **(e)(3)**: Incorporated language to reference Regulation 1541.5 regarding printed sales messages.

ACTION 4 – Definition of Contract of Sale – (a)(4) - Page 4

Contract of sale is defined to explain which documents and agreements will govern the sales of tangible personal property to the client. The master agreement is not necessarily the same thing in that it encompasses the entire relationship between the agency and its client. Both need to be defined.

ACTION 5 – Definition of Finished Art – (a)(7) - Page 7

Mr. Wayne proposes to clarify the definition of finished art by adding a reference to the preparation of special printing aids. AAA proposes inserting a reference to advertising agencies after "environmental graphic design services." Staff does not agree that this definition needs clarification. Staff believes that the term is accurately and clearly defined.

ACTION 6 – Definition of Intermediate Production Aids – (a)(9) - Page 8

Mr. Wayne proposes to clarify the definition of intermediate production aids. Staff does not agree that this definition needs clarification. Staff believes that the term is accurately and clearly defined. AAAA proposes to include clip-art and eliminate artwork in the definition of intermediate production aids. Staff does not agree with AAAA because considering clip-art as an intermediate production aid would make it taxable when currently clip-art alone is considered typography (i.e., not taxable).

ACTION 7 – Definition of Preliminary Art – (a)(11) – Page 8

Mr. Wayne proposes to imply that the same business entity that prepared the preliminary art also prepared the finished art. Staff believes that the proposed changes could be misread to mean that charges for preliminary art are taxable if no final art is ever delivered. Staff believes the wording of the regulation pertaining to preliminary art is correct and complete as drafted. AAAA proposes an alternative definition of preliminary art in that it is incidental to the design services provided and not subject to tax. Staff believes that the AAAA's definition is contradictory and eliminates the entire concept of preliminary art that is created prior to approval, which is a long-standing rule. The true object of the contract is the finished art and under AAAA's proposal, all charges for preliminary art would be taxable if finished art is delivered. The application of tax does not belong in the definition and would clearly be misleading here (see AAAA's own language in subdivision (c)(1)(A)).

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ACTION 8 – Application of Tax to Services – Passage of Title – (b)(1)(A)1. &2. – Pages 10-13

(b)(1)(A)1.: Mr. Wayne proposes to incorporate the concept of a “killed job” when preliminary art does not result in the client’s approval. Staff believes that including such language could be misleading, and appears to be inconsistent with language proposed by Mr. Wayne for subdivision (b)(1)(A)2. AAAA proposes alternative language that preliminary art is incidental. Staff does not agree that preliminary art is incidental and not subject to tax as noted in the Action 7 comment. However, AAAA notes that preliminary art may be taxable if the advertising agency or commercial artist, in the master agreement, passes title or the right to permanent possession to the client. This does not appear to be consistent with their definition of preliminary art. Staff did incorporate the language “master agreement or other contract” into this section. There is no reason to strike the title provision language at the end of this subdivision. AAAA’s language is confusing and not as concise and clear as staff’s language and appears to be inconsistent with its own proposed definition of preliminary art.

(b)(1)(A)2.: Mr. Wayne proposes to clarify that an advertising agency or commercial artist can act as a retailer by means of a title clause in the contract of sale that passes title to the client prior to use. Staff believes that including such language could be misleading, and therefore recommends against including this language in the regulation.

ACTION 9 – Specific Nontaxable Charges – (b)(1)(F) – Page 15

Mr. Wayne proposes to categorize specific nontaxable charges as “markup” and include language on nontaxable agent fees. Staff believes that the added language is not appropriate for subdivision (b)(1)(F). The proposed terminology is incorrect in that the term “markup” normally connotes a taxable component. Staff believes that a fee for acting as an agent for the purchase of tangible personal property would never come within this provision because it would never be a nontaxable agency fee if related to a sale of tangible personal property by the advertising agency or commercial artist. Staff believes that the discussion of the application of tax to agency fees belongs in the part of the regulation that pertains to such activities. Such agency fees arise only when an advertising agency acts as an agent of its client for the purpose of obtaining tangible personal property, and this topic is covered in subdivision (c)(1). Staff believes its language in subdivision (c)(1)(B) adequately addresses services provided by an advertising agency and commercial artists acting as agents.

ACTION 10 – Use of Aids in Creation of Finished Art – Title Clause Agreement – (b)(2)(A) – Page 18

AAAA’s proposed language is not clear on what “taxed only once” means and uses incorrect terminology. This topic requires the extensive discussion provided by Regulation 1541, and the previous paragraph refers to that regulation. Rather than repeat that entire discussion so that this topic is fully and properly covered, it is preferable for the reader to go to Regulation 1541 for a complete explanation.

ACTION 11 – Transfer of Finished Art in Tangible Form – Cost of Special Printing Aids – (b)(2)(C) – Page 23

AAAA deletes an important concept that tax is due on at least cost of the finished art, intermediate production aids and special printing aids, to the advertising agency or commercial artist. Deleting this statement would mislead the reader since the presumption would always be overcome if the cost is greater than 25 percent. This statement simply puts the reader on notice of the correct application of the presumption.

ACTION 12 – Transfer of Finished Art in Tangible Form – Option to Separately State Special Printing Aids – (b)(2)(C) – Page 23

Mr. Wayne proposes to provide clarifying language that there is an option to separately state intermediate production aids as a retail sale or as an agent transaction. Staff believes that this proposed language is not appropriate in this subdivision since the purpose of subdivision (b)(2)(C) is to address charges for finished art that are combined with charges for conceptual design.

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ACTION 13 – Technology Transfer Agreement – Requirement That It Be in Writing – (b)(2)(D)2. – Page 23

Mr. Liao proposes that a technology transfer agreement does not have to be in writing, since the statute states “any agreement.” Staff addressed this issue in proposed Regulation 1507 which has been approved for publication with the writing evidence requirement.

ACTION 14 - Technology Transfer Agreement – Finished Art Transferred on Computer Storage Media - (b)(2)(D)2. – Page 24

Guild proposes to clarify that finished artwork temporarily transferred on computer storage media in a technology transfer agreement has a de minimis fair rental value and that the value of the artwork is incidental to the transfer of intangible rights. Staff believes that RTC section 6011(c)(10) and 6012(c)(10) explicitly set forth the measure of tax on the sale of tangible personal property in connection with the technology transfer agreement.

ACTION 15 – Technology Transfer Agreement – Separately Stated Price - (b)(2)(D)2.a – Page 25

Mr. Blonder proposes to add language referencing a separately stated rent for temporary possessions of finished art. Staff agrees that the language “sales price” applies to a lease as a continuing sale but believes that the added language is not necessary and redundant because the concept is already covered by the term “sales price.”

ACTION 16 - Technology Transfer Agreement – The Value of the Artist’s Labor - (b)(2)(D)2.c – Page 26

The Guild and Mr. Blonder believe that the value of labor should only include the labor purchased from a third party or paid to an employee. Each proposes separate language. Staff does not agree that the labor of an individual artist has no value. Staff believes that the implied and opportunity costs are included in the cost of labor calculation.

The Guild proposes that if staff’s recommendation is adopted, in the absence of an objective verifiable measure of labor cost, it should be presumed that the fair market value of the labor is \$100. Staff believes that the fair market value of the artist’s time will vary significantly from job to job and that the \$100 presumption may not be representative.

ACTION 17 – Cost of Materials – Includes Those Used as Well as Incorporated – (b)(2)(D)2.c. – Page 26

Mr. Liao proposes language to provide that the “cost of materials” are only those that are physically incorporated into the finished art. Staff believes that both materials used and incorporated into the finished art are included in the cost of materials.

ACTION 18 – Explanation of Calculation of Sales Price of Other Tangible Personal Property – (b)(3) – Page 27

Staff does not agree with AAAA’s proposal to delete this subdivision because this deletion would remove the explanation of the application of tax to sales of other tangible personal property, which is not covered in AAAA’s proposed language.

ACTION 19 – Evidence to Prove Erroneous Issuance of Resale Certificate – (c)(1)(C) –Pages 31 and 32

AAAA’s proposed version would make the presumption irrebuttable. Currently, the presumption is intended to apply to both the purchasing for resale *and* not purchasing as an agent. AAAA’s language would limit the presumption to the purchasing for resale and would state, as a fact, that the agency does not act as an agent, thus making the presumption irrebuttable. This issue arises when the agency collects no tax reimbursement from its client but had issued a resale certificate. The agency may show that the certificate was issued in error and that it did not treat the transaction as a purchase for resale to its client. However, if the agency bills the client for tax which the client pays, then the agency did treat the transaction as one for resale and thus cannot show that the issuance of the certificate was in error. The purpose for including this statement is so that the regulation includes a complete statement of the administration of this provision.

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ACTION 20 – Invoice to Client for More Than Cost of Property – (c)(2)(C) – Pages 36-37

Staff does not agree with AAAA’s proposal to delete this subdivision because the deletion would remove the explanation of the application of tax to lump-sum retail sales of tangible personal property by advertising agencies. The AAAA’s proposed language provides no guidelines for these types of transactions.

ACTION 21 – General Language Differences

Page 1 – **(a)(1)**: “Person,” which is already defined for purposes of the Sales and Use Tax Law, is an all-inclusive term. “Entity” is not defined, and its addition here would be redundant and confusing.

Page 2 – **(a)(2)**: Staff included the additional examples “media planning” and “public relations.” The list of services is intended to be a representative list, not an exhaustive list.

Pages 2-3 – **(a)(3)**: The definition of “commercial artists” was rewritten to include all relevant persons, including both designers and commercial photographers, in order to make the regulation easier to read. Otherwise, the addition of commercial photographers as well would have made the constant references to the persons covered by the regulation ungainly. As proposed by staff, designers are clearly covered.

Pages 6-7 – **(a)(6)**: Staff added a separate definition for “third parties” in subdivision (a)(13). The definition includes a transfer to a third party on the client’s behalf. Staff did not change the definition of electronic artwork. The point of defining electronic artwork is to explain that it is in digital format. Changing it here is directly contrary to the reference in (a)(3). It also negates the need for (b)(2)(B) since electronic artwork would never be tangible.

Page 7 – **(a)(7)**: AAAA proposes adding “advertising agencies” after “environmental graphic design services” in the last sentence of the definition of finished art. Staff does not agree with AAAA since an advertising agency is not an architect and should not be referenced here.

Page 10 – **(b)(1)(A)1.**: Staff did not change language in the second sentence, and the grammatical change is not necessary.

Page 14 – **(b)(1)(B)**: Staff incorporated the principle with modified language.

Page 15 – **(b)(1)(F)**: Staff believes its language is clearer with the reference to subdivision (b)(3). Staff believes that AAAA’s proposed deletion defeats the primary purpose for this provision, which is to explain which fees are *not* taxable as part of direct labor when calculating taxable measure.

Pages 15-16 – **(b)(1)(F)1. & 2.**: Staff believes that adding the language “or fees” to commissions is redundant and unnecessary. The point is already fully and more properly covered in the introductory paragraph for this subdivision that references “similar fees and commissions.”

Page 18 – **(b)(2)(B)**: Staff does not believe there is a need to add “Electronic Artwork” to the title of the subdivision.

Page 20 – **(b)(2)(B)**: Not only are the first suggested additions not in conformity with the terminology of the rest of the regulation, staff believes there is no need for such additional language. Also, staff believes that a signature should be obtained at the time of loading rather than initials after the fact at the point of invoicing.

Page 21: **(b)(2)(C)**: Staff believes its language is clearer.

Page 25: **(b)(2)(D)2.a.**: The Guild proposes to clarify that the measure of tax on a transfer of finished art is a “reasonable” value, not a “fair market value.” Staff believes that the “fair market value” is a valid interpretation of the statutes in determining what constitutes “reasonable” for purposes of this subdivision.

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ACTION 21 – General Language Differences (continued)

Page 27: **(b)(2)(D)2.c.**: AAAA proposes to add the following sentence “Nontaxable fees, charges and commissions are not included in the calculation of direct labor.” This point is clearly made previously in the regulation in the area where the calculation of direct labor is discussed in subdivision (b)(1)(F) and is not needed here.

Page 29: **(b)(4)**: Staff believes this subdivision should not be deleted. The language provides an explanation of the application of tax to purchases of supplies consumed in the business operation. This is a general sales and use tax application.

Page 30 - **(c)(1)**: Staff’s version is more specific and helpful to the reader.

Page 31 - **(c)(1)(A)**: Staff’s version is more specific and helpful to the reader.

Page 34 - **(c)(2)(A)**: Tax is always due on the taxable selling price of tangible personal property, so the reference to “except for” is legally incorrect. The term “taxable selling price” is also not defined. Artwork done in-house is fully discussed in subdivision (b)(2)(B).

Page 35 - **(c)(2)(B)**: Mr. Wayne suggests that a definition of “incorporated” be included in the regulation. Staff feels that an explanation at this level of detail is more appropriately included in subsidiary materials, such as a Tax Tip pamphlet. AAAA suggests that tax applies to sales of tangible personal property “except for in-house artwork.” Staff notes that tax is always due on the taxable selling price of tangible personal property, so the reference to “except for” is legally incorrect. The term “taxable selling price” is also not defined.

Page 38 - **(e)(5)**: Staff believes its version is correctly stated. The taxability of the transactions is based on the conditions that exist in each transaction as specifically discussed in Regulation 1529. AAAA’s language may mislead the reader who should be simply directed to Regulation 1529 for a complete discussion of the topic.

Regulation 1540. ADVERTISING AGENCIES AND COMMERCIAL ARTISTS.

Reference: Sections 6006 - 6015, Revenue and Taxation Code.

(a) DEFINITIONS.

(1) **ADVERTISING.** Advertising is commercial communication utilizing one or more forms of communication (such as television, print, billboards, or the Internet) from or on behalf of an identified person **or entity** to an intended target audience.

(2) **ADVERTISING AGENCIES.** Advertising agencies design and implement advertising campaigns for purposes of advertising the goods, services, or ideas of their clients. As part of that primary function, advertising agencies provide their clients with services (such as consultation, consumer research, and media placement, **media planning, television and radio commercials, print advertising, brand advertising, website design, internet design public relations and development of marketing communication programs**). ~~and tangible personal property (such as print advertisements, finished art, and video and audio productions).~~ **Incidental to these services, the advertising agencies may provide some tangible personal property to the client.**

(3) **COMMERCIAL ARTISTS AND DESIGNERS.** Commercial artists, who may characterize themselves as commercial artists, commercial photographers, or designers, provide services and tangible personal property to their clients for use in their clients' advertising campaigns, or for their clients' other commercial endeavors such as sales of copies of finished art (including, e.g., photographic images) provided by a commercial artist. Services they provide to their clients include the creation and development of ideas, concepts, looks, or messages. Electronic artwork they provide may be transferred through remote telecommunications such as by modem or over the Internet, or by tangible means through electronic media such as compact or floppy disc. Tangible personal property they provide may include electronic media on which electronic artwork is transferred to the client, hard copies of the electronic artwork, hard copies of finished art (which may consist of photographic images).

~~-(4) **CONTRACT OF SALE.** An agreement to transfer tangible personal property for consideration is a contract of sale. A contract of sale consists of all terms comprising the obligation of the parties for the sale and purchase of the tangible personal property in question. A contract of sale may consist of a single contract document. A contract of sale may also consist of multiple documents. For example, a master agreement between an advertising agency and its client may specify the obligations of each with respect to the design of an advertising campaign for the client, the placement of the advertising with print and television media, and for the sale and purchase of tangible personal property related to the advertising campaign. There may then be additional terms for the purchase of specific tangible personal property during the advertising campaign, such as in a purchase order, which identifies the specific property that will be purchased and sold and the sales price for that property. In this example, not all terms of the sale and purchase of the tangible personal property identified in the purchase order are included in~~

~~the master agreement, nor are all terms included in the purchase order. Rather, the contract of sale in this circumstance consists of the relevant provisions of the master agreement as modified by the specific provisions in the purchase order.~~

(5) **ELECTRONIC ARTWORK.** Electronic artwork is artwork created through the use of computer hardware and software processes which results in artwork in a digital format that can be transmitted to ~~others the client or a third party~~ via electronic means (that is, transmitted through remote telecommunications such as by modem or over the Internet, or by electronic media such as compact or floppy disc). Elements of the process include the creation of original artwork or photographic images, scanning of artwork or photographic images, composition and design of text, insertion and manipulation of scanned and original electronic artwork, photographic images, and ~~or text~~. Electronic artwork does not include artwork that is transferred to customers in a tangible form, **such as compact or floppy disc, other than on electronic media,** ~~even where such artwork may have been manufactured or produced in whole or in part by computer hardware and software processes.~~

(6) **FINISHED ART.** Finished art is the final artwork used for actual reproduction by photomechanical or other processes, or used for display. It includes electronic artwork, illustrations (e.g. drawings, diagrams, halftones, or color images), photographic images, sculptures, paintings, and handlettering. Blueprints, diagrams, and instructions for signage furnished to a client as the result of environmental graphic design services **or advertising agencies** are not finished art.

(7) **HARD COPIES.** An item is transferred on hard copy when it is transferred on any tangible personal property other than in digital format on electronic media. For example, finished art transferred on canvas or paper is transferred on hard copy while a transfer of finished art in digital format on compact or floppy disc is not regarded as a transfer on hard copy.

(8) **INTERMEDIATE PRODUCTION AIDS.** Intermediate production aids include items such as ~~artwork~~, **clip-art (pre-packaged art)**, illustrations, photograph images, photo engravings, and other similar materials which are used to produce special printing aids or other intermediate production aids.

(9) **MASTER AGREEMENT.** A master agreement is a contract, however characterized (such as "agency-client agreement"), entered into between an advertising agency or commercial artist and its client which specifies the obligations of each party to the master agreement with respect to their relationship, whether for a specified time or advertising campaign or until one of the parties terminates the agreement. After entering into a master agreement, the parties may thereafter enter into additional contracts, including fulfillment of purchase orders issued by the client for the purchase of specific services, tangible personal property, or both, which additional contracts include all the terms in the master agreement which are not explicitly in conflict with the later contracts.

(10) **PRELIMINARY ART.** ~~Preliminary art is tangible personal property which is prepared solely for the purpose of demonstrating an idea or message for acceptance by the client before a contract is entered into or before approval is given for preparation of finished art to be furnished or licensed by the seller~~ **advertising agency, artist or designer** to his or her client, provided neither title to nor permanent possession of such tangible personal property passes to the client. **Preliminary art consists of creative art services whose object is to convey ideas for review by the client and as such, any tangible personal property, is incidental to the true object of the transaction.** Preliminary art may include, **but is not limited to**, roughs, visualizations, layouts, comprehensives, and instant photos. **Preliminary art is not subject to tax.**

(11) **SPECIAL PRINTING AIDS.** Special printing aids are reusable manufacturing aids which are used by a printer during the printing process and are of unique utility to a particular customer. Special printing aids include electrotypes, stereotypes, photo engravings, silk screens, steel dies, cutting dies, lithographic plates, film, single or multi color separation negatives, and flats.

(b) SITUATIONS SPECIFIC TO ADVERTISING AGENCIES

(1) ADVERTISING AGENCY ACTING AS AN AGENT FOR ITS CLIENT. An agent is one who represents another, called the principal, in dealings with third persons. (Civil Code section 2295). To the extent that an advertising agency acts as the agent of its client when acquiring tangible personal property, it is neither a purchaser of the property with respect to the supplier nor a seller of the property with respect to its principal (that is, its client). Because of the unique relationship between advertising agencies and its clients, unless the advertising agency elects non-agent status ~~under subdivision (b)(2), or is otherwise the retailer of the property under subdivision (c)(2)(B) or (c)(2)(C)~~ it is rebuttably presumed that the advertising agency acts as an agent of its client acquiring tangible personal property on its client's behalf **(see (c)(2)(A),(B),(C)).**

(A) A supplier of tangible personal property to an advertising agency is presumed to have made a retail sale of that property unless the supplier takes a timely and valid resale certificate in good faith from the advertising agency. Otherwise, the supplier has the burden of establishing that the advertising agency elected non-agent status ~~under subdivision (c)(2)(A)~~ and resold the property or that the advertising agency resold the property as the retailer ~~under subdivision (c)(2)(B) or (c)(2)(C).~~

(B) When an advertising agency is the agent of its client for the purchase of tangible personal property under subdivision (b) (1), sales or use tax is due on the purchase price from the supplier to the advertising agency. Tax does not apply to the charge made by the advertising agency to its client for reimbursement, including tax reimbursement,

for

the amount charged by a supplier nor does tax apply to the advertising agency's separately stated charges for its services directly related to its acquisition of such tangible personal

property (e.g., when the advertising agency makes a separately itemized charge for reimbursement of the amount paid to the supplier of the property, tax does not apply to a separately itemized "agency fee"). When the applicable tax is use tax and the advertising agency does not pay that use tax to the supplier on the client's behalf, the advertising agency is liable for the use tax and must report and pay the use tax to the Board. The advertising agency's liability for that use tax is not extinguished unless the client has self-reported and paid tax to the Board.

(C) An advertising agency may not issue a resale certificate when purchasing tangible personal property as the agent of its client. An advertising agency who issues a resale certificate to a supplier is presumed to be purchasing tangible personal property from that supplier on its own behalf for resale and ~~is not to be~~ acting as an agent of its client. However, the advertising agency may provide evidence to prove that its issuance of the resale certificate was erroneous and that the advertising agency was acting as an agent of its client. ~~provided the advertising agency has not treated the transactions as its own sale of tangible personal property or its client, collecting tax or tax reimbursement from its client on that sale.~~ If the resale certificate was issued in error, the advertising agency is liable for use tax on the cost of tangible personal property purchased under the certificate unless the advertising agency has already paid that tax to the supplier or to the Board, or the client has self-reported and paid the tax to the Board.

(2) **ADVERTISING AGENCY ACTING AS A RETAILER.** An advertising agency that acts as a retailer of tangible personal property may issue a resale certificate for such tangible personal property if the property will be resold prior to any use.

agent (A) **ELECTION OF NON-AGENT STATUS.** An advertising agency may elect non-agent status with respect to sales of tangible personal property to its client. This election must be supported by a specific written statement in its master agreement with the client. Alternatively, a statement may be included on an advertising agency's job order or invoice to its client. Statements should include the following or similar language: "(Advertising Agency's name) will not be acting as an agent of (client's name) for purposes of this transaction."

An advertising agency that elects non-agent status is a retailer with respect to tangible personal property sold to its clients. The measure of tax on the advertising agency's retail sale is the separately stated charge for the tangible personal property. If there is no such separately stated charge, the measure of tax is calculated as provided in subdivision (c).

Except for in-house artwork billed on a lump sum method under section (c) (5), tax is due on the taxable selling price of tangible personal property . If there is no separately stated charge, the taxable selling price may be calculated as shown in subdivision (c).

(B) **ITEMS PRODUCED OR FABRICATED BY AN ADVERTISING AGENCY**

IN-HOUSE. Advertising agencies are retailers of tangible personal property they produce or fabricate, e.g., by their own employees. Advertising agencies are not agents of their clients with respect to the acquisition of materials incorporated into such items of tangible personal property they produce or fabricate, but instead are the retailers of such property. The measure of tax on their retail sale of that property is the separately stated charge for the property sold. If there is no such separately stated charge, the measure of tax is calculated as provided in subdivision (c).

Except for in-house artwork billed as a lump-sum under section (c)(5), tax is due on the taxable selling price of tangible personal property fabricated or produced by the advertising agency's employees. In those situations, an advertising agency should issue a resale certificate when purchasing items that become part of such tangible personal property.

(c) APPLICATION OF TAX TO ACTIVITIES OF ADVERTISING AGENCIES AND COMMERCIAL ARTISTS.

(1) SERVICES.

(A) GENERAL.

1. Services performed to convey ideas, concepts, looks, or messages to a client may result in a transfer, enhancement, or revision of either electronic artwork, hard copies of electronic artwork, or copies of manually prepared artwork. ~~If Charges for such services are separately stated as are nontaxable if separately stated as “design charges,” “preliminary art,” “concept development,” or any other designation that clearly indicates that the charges are for such services and not for finished art. The transfer of tangible personal property from the advertising agency, artist or designer is incidental to the service provided and not subject to tax. However, if the master agreement provides that the advertising agency, artist or designer will pass to the client title or the right to permanent possession of the artwork in tangible form such as electronic media, or hard copy or permanent possession of the artwork in tangible form is in fact, transferred to the client, then tax is applicable. they are nontaxable unless the contract of sale provides that the advertising agency or commercial artist will pass to the client title or the right to permanent possession of the artwork in tangible form, such as on electronic media or hard copy, or permanent possession of the artwork in tangible form is, in fact, transferred to the client.~~

~~However,~~ If the ~~contract~~ master agreement provides that the client owns the concepts embodied in tangible personal property that is owned and possessed by the advertising agency or commercial artist (e.g., so that such concepts cannot be used on behalf of any other person), that ~~contract~~ master agreement provision does not constitute the passage of title to tangible personal property to the client, provided the client does not thereby obtain the actual title to, or permanent possession of, the tangible personal property embodying the concepts. A requirement that an advertising agency or commercial artist retain permanent possession of the artwork in tangible

form does not itself constitute a sale of that property to the client. ~~in the absence of a provision passing title to such property to the client.~~

2. Tangible personal property developed and used during services performed to convey ideas, concepts, looks, or messages is consumed in the performance of those services. Unless, prior to any use, the advertising agency or commercial artist passes title to such property to the client as discussed in the previous paragraph, the advertising agency or commercial artist is the consumer of such tangible personal property used and tax applies to the sale of property to, or to the use of the property by, the advertising agency or commercial artist. If the advertising agency or commercial artist passes title to, or permanent possession of, such tangible personal property to its client, tax applies to the sale of the tangible personal property by the advertising agency or commercial artist **to the client.**

(B) DIGITAL PRE-PRESS INSTRUCTION. A file prepared to the special order of the client which qualifies as digital pre-press instruction as defined in subdivision (f) of Regulation 1541 is a custom computer program, and its transfer is not subject to tax regardless of the form in which the file is transferred or the time at which it is transferred. **Electronic or digital pre-press instruction shall not, however, be regarded as a custom computer program if it is a "canned" or prewritten computer program which is held or existing for general or repeated sale or lease, even if the electronic or digital pre-press instruction was initially developed on a custom basis or for in-house use. In such cases, the "canned" software is taxable.**

(C) RETOUCHING PHOTOGRAPHIC IMAGES. Retouching a photographic image for the purpose of repairing or restoring the photograph to its original condition is a repair, the charge for which is not taxable.

(D) SIGNAGE. The creation and providing of single copies of blueprints, diagrams, and instructions for signage as a result of environmental graphic design is a service the charge for which is not taxable. Charges for additional copies are taxable.

(E) WEBSITES. The design, editing, or hosting of an electronic website in which no tangible personal property is transferred to the client is a service, the charge for which is not subject to tax.

(F) SPECIFIC NONTAXABLE CHARGES. The following , and similar fees and **commissions, are** not taxable when they are separately stated. ~~Whether separately stated or not, these fees and commissions are not included in the calculation of "direct labor" for purposes of subdivision (b)(3).~~

1. Media commissions **or fees** received for placement of advertising whether paid by the medium, by another advertising agency, or by the client.

2. Commissions **or fees** paid to advertising agencies by suppliers. Examples of such commissions are those paid to an advertising agency by a premium manufacturer (or distributor) or a direct-by-mail supplier.

3. Consultation and concept development fees related to client discussion, development of ideas, and other services. If the advertising agency transfers to the client tangible personal property produced as a result of these services, the transfer is incidental to the advertising agency's providing of the service and is not a sale of that tangible personal property; the advertising agency is the consumer of tangible personal property transferred to the client incidental to the providing of a service.

4. Fees for research or account planning that entail consumer research and the application of that research to the client's business or industry.

5. Fees for quality control supervision that entails the proofing and review of printing and other products provided by outside suppliers.

6. Charges for the formulation and writing of copy.

(2) FINISHED ART.

(A) **USE OF AIDS IN CREATION OF FINISHED ART.** If the advertising agency or commercial artist uses any intermediate production aids or special printing aids in the creation of the finished art, the presumptions with respect to passage of title and the calculation of the measure of tax on the sale of such aids by the advertising agency or commercial artist, is governed by the provisions of Regulation 1541 applicable to special printing aids.

(1) Prior to the preparation of finished art, if the client signs a title clause agreement to purchase intermediate production aids or obtain the lease rights for illustrations, electronic art, photography, typography, airbrushing, photo retouching, filmwork, photostats, dies, lithographic film and plates, photo engravings, and other materials needed to prepare the finished artwork, the intermediate production aids are taxed only once.

(B) **TRANSFERS OF FINISHED ART NOT IN TANGIBLE FORM. (ELECTRONIC ARTWORK).** A transfer of electronic artwork from an advertising agency or commercial artist to the client or to a third party on the client's behalf that is not in tangible form is not a sale of tangible personal property, and the charges for the transfer are not subject to tax. A transfer of electronic artwork is not in tangible form if the file containing the electronic artwork is transferred through remote telecommunications (such as by modem or over the Internet), or if the file is loaded into the client's computer by the advertising agency or commercial artist, and the client does not obtain title to or possession of any tangible personal property, such as electronic media or hard copy. If the transfer is not a transfer in tangible form because it is loaded onto the client's computer, the advertising agency or commercial artist should document that transfer by a

written statement signed at the time of loading by the client and by the person who loaded the electronic artwork into the client's computer with the following or similar language: "This electronic artwork was loaded into the computer of [client's name] by [seller's name], **(advertising agency, artist or designer's name)** and [seller's name] **(advertising agency, artist or designer's name)** did not transfer any tangible personal property containing the artwork, such as electronic media or hard copies, to [client's name]." When such a statement is signed **or initialed** at the time the file is loaded **or at the point the transfer is invoiced to the client**, it will be rebuttably presumed that the transfer of electronic artwork was not transferred in tangible form. If there is no such timely completed statement, the advertising agency or commercial artist may provide other substantive evidence establishing that the artwork was not transferred in tangible form.

(C) **TRANSFERS OF FINISHED ART IN TANGIBLE FORM.** The electronic or manual preparation of finished art for use in reproduction or display is not a service. ~~Unless the transfer is not in tangible form as explained in subdivision (b)(2)(B),~~ The transfer of finished art **in tangible form** is a sale of tangible personal property and tax applies to charges for that finished art, including all charges for any rights sold with the finished art such as copyrights or distribution and production rights, except as provided in subdivision (b)(2)(D)2. ~~If charges for finished art are combined into a single charge that also includes nontaxable charges for conceptual services described in subdivision (b)(1)(A), the advertising agency or commercial artist may report the measure of tax on the retail sale of the finished art as specified in subdivision (b)(3), provided that the reported measure of tax must also include the value of reproduction rights included with the transfer except those that are not taxable as provided in subdivision (b)(2)(D)2.~~

(1) LUMP SUM BILLING OF IN-HOUSE ARTWORK CONTAINING PRELIMINARY ART AND FINISHED ART.

An advertising agency, artist or designer may elect to do a lump-sum billing of in-house artwork containing both preliminary art and finished art.

~~If tax is not reported on this basis,~~ **On billing of in-house artwork for which an**

advertising agency, artist or designer makes a lump-sum charge that includes both preliminary art and other nontaxable services and finished art, it will be rebuttably

presumed that 75 percent of the combined charge for the finished art and conceptual services is for the nontaxable services and that 25 percent of the combined charge is the

measure of tax on the retail sale of the finished art, provided that 25 percent of the

combined charge is not less than the sales price to the advertising agency or commercial artist of the finished art (or component parts) and any intermediate production aids or

special printing aids sold to the client. ~~If such sales price to the advertising agency or~~

~~commercial artist is more than 25 percent of the combined charge to the client, the~~

~~measure of tax shall be deemed to be such sales price of the tangible personal property to~~

~~the advertising agency or commercial artist.~~

(D) REPRODUCTION RIGHTS TRANSFERRED WITH FINISHED ART.

1. Charges for the transfer of possession in tangible form to the client or to anyone else on the client's behalf of finished art for purposes of reproduction are included in the measure of tax on that sale, including all charges for the right to use that property, even though there is no transfer of title to the person reproducing the finished art, except as provided in subdivision (b)(2)(D)2.

2. Any agreement evidenced by a writing (such as a contract, invoice, or purchase order) that assigns or licenses a copyright interest in finished art for the purpose of reproducing and selling other property subject to the copyright interest is a technology transfer agreement, as explained further in Regulation 1507. Tax applies to amounts received for any tangible personal property transferred as part of a technology transfer agreement. Tax does not apply to amounts received for the assignment of a copyright interest to a third party as part of a technology transfer agreement. The measure of tax on the sale of finished art transferred by an advertising agency or commercial artist as part of a technology transfer agreement shall be:

a. The separately stated sales price for the finished art, provided the separately stated price represents a reasonable fair market value of the tangible personal property;

b. Where there is no such separately stated price, the separate price at which the person holding the copyright interest in the finished art has sold or leased like property to an unrelated third party without also transferring an interest in the copyright. This paragraph does not apply if the person holding the copyright interest has not sold or leased like property without also transferring an interest in the copyright; or

c. If there is no such separately stated price under subdivision (b)(2)(D)2.a., nor a separate price under subdivision (b)(2)(D)2.b., 200 percent of the combined cost of materials and labor used to produce or acquire the finished art. "Cost of materials" consists of the costs of those materials used or incorporated into the finished art, or any tangible personal property transferred as part of the technology transfer agreement. "Labor" includes any charges or value of labor used to create such tangible personal property whether the advertising agency or commercial artist performs such labor, a third party performs the labor, or the labor is performed through some combination thereof. The value of labor provided by the advertising agency or commercial artist shall equal the lower of the normal and customary charges for labor billed to third parties by the advertising agency or commercial artist, or the fair market value of the labor performed by the advertising agency or commercial artist. **Nontaxable fees, charges and commissions are not included in the calculation of direct labor (see (c) (1) (f)).**

~~-(3) SALES OF OTHER TANGIBLE PERSONAL PROPERTY BY ADVERTISING AGENCY OR COMMERCIAL ARTIST. Tax applies to the total charge for the retail sale of tangible personal property by an advertising agency or commercial artist. If an advertising agency or commercial artist combines charges for nontaxable services as defined in subdivision (b)(1)(F), such as media placement, with charges for tangible personal property for which the advertising agency or commercial artist is the retailer, the measure of tax on that retail sale of property includes the total of: direct labor; the cost of purchased items that become an ingredient or component part of the tangible personal property; the cost of any intermediate production aids~~

~~or special printing aids; and a reasonable markup. Commissions, fees, and other charges exclusively related to the production or fabrication of tangible personal property are part of direct labor and are thus included in the measure of tax. Such charges include retouching of photographic images or other artwork for reproduction, provided the retouching is intended to improve the quality of the reproduction. An advertising agency or commercial artist must keep sufficient records to document the basis for the reported measure of tax.~~

~~-(4) ITEMS PURCHASED BY AN ADVERTISING AGENCY OR COMMERCIAL ARTIST. Except when property is resold prior to any use, an advertising agency or commercial artist is the consumer of tangible personal property used in the operation of its business. Tax applies to the sale of such property to, or to the use of such property by, the advertising agency or commercial artist.~~

~~(c) SITUATIONS SPECIFIC TO ADVERTISING AGENCIES.~~

~~(1) ADVERTISING AGENCY ACTING AS AN AGENT FOR ITS CLIENT. An agent is one who represents another, called the principal, in dealings with third persons. (Civil Code section 2295.) To the extent that an advertising agency acts as the agent of its client when acquiring tangible personal property, it is neither a purchaser of the property with respect to the supplier nor a seller of the property with respect to its principal (that is, its client). Because of the unique relationship between advertising agencies and their clients, unless an advertising agency elects non-agent status under subdivision (c)(2)(A) or is otherwise the retailer of the property under subdivision (c)(2)(B) or (c)(2)(C), it is rebuttably presumed that the advertising agency acts as the agent of its client when acquiring tangible personal property on its client's behalf.~~

~~(A) A supplier of tangible personal property to an advertising agency is presumed to have made a retail sale of that property unless the supplier takes a timely and valid resale certificate in good faith from the advertising agency. Otherwise, the supplier has the burden of establishing that the advertising agency elected non-agent status under subdivision (c)(2)(A) and resold the property or that the advertising agency resold the property as the retailer under subdivision (c)(2)(B) or (c)(2)(C).~~

~~(B) When an advertising agency is the agent of its client for the purchase of tangible personal property under subdivision (c)(1), sales or use tax is due on the purchase price from the supplier to the advertising agency. Tax does not apply to the charge made by an advertising agency to its client for reimbursement, including tax reimbursement, for the amount charged by a supplier, nor does tax apply to the advertising agency's separately stated charges for its services directly related to its acquisition of such tangible personal property (e.g., when the advertising agency makes a separately itemized charge for reimbursement of the amount paid to the supplier of the property, tax does not apply to a separately itemized "agency fee"). When the applicable tax is use tax and the advertising agency does not pay that use tax to the supplier on the client's behalf, the advertising agency is liable for the use tax and must report and pay the use tax to the Board. The advertising agency's liability for that use tax is not extinguished unless the client has self-reported and paid the tax to the Board.~~

~~(C) An advertising agency may not issue a resale certificate when purchasing tangible personal property as the agent of its client. An advertising agency who issues a resale certificate to a supplier is presumed to be purchasing tangible personal property from that supplier on its own behalf for resale and not to be acting as an agent of its client. However, the advertising agency may provide evidence to prove that its issuance of the resale certificate was erroneous and that the advertising agency was acting as an agent of its client, provided the advertising agency has not treated the transaction as its own sale of tangible personal property to its client, collecting tax or tax reimbursement from its client on that sale. If the resale certificate was issued in error, the advertising agency is liable for use tax on the cost of tangible personal property purchased under the certificate unless the advertising agency has already paid that tax to the supplier or to the Board, or the client has self-reported and paid the tax to the Board.~~

~~(2) ADVERTISING AGENCY ACTING AS A RETAILER. An advertising agency that acts as a retailer of tangible personal property may issue a resale certificate for such tangible personal property if the property will be resold prior to any use.~~

~~(A) ELECTION OF NON AGENT STATUS. An advertising agency may elect non agent status with respect to sales of tangible personal property to its client. This election must be supported by a specific written statement in its master agreement with the client. Alternatively, a statement may be included on an advertising agency's job order or invoice to its client. Statements should include the following or similar language: "(Advertising Agency's name) will not be acting as an agent of (client's name) for purposes of this transaction."~~

~~An advertising agency that elects non agent status is a retailer with respect to tangible personal property sold to its clients. The measure of tax on the advertising agency's retail sale is the separately stated charge for the tangible personal property. If there is no such separately stated charge, the measure of tax is calculated as provided in subdivision (b).~~

~~(B) ITEMS PRODUCED OR FABRICATED BY AN ADVERTISING AGENCY IN-HOUSE. Advertising agencies are retailers of tangible personal property they produce or fabricate, e.g., by their own employees. Advertising agencies are not agents of their clients with respect to the acquisition of materials incorporated into such items of tangible personal property they produce or fabricate, but instead are the retailers of such property. The measure of tax on their retail sale of that property is the separately stated charge for the property sold. If there is no such separately stated charge, the measure of tax is calculated as provided in subdivision (b).~~

~~(C) INVOICE TO CLIENT FOR MORE THAN COST OF TANGIBLE PERSONAL PROPERTY TO ADVERTISING AGENCY. When an advertising agency invoices its client for tangible personal property provided by the advertising agency without separately stating the amount of paid to the supplier for that property, the advertising agency is the retailer of the tangible personal property to its client. For example, when the advertising agency invoices a single charge to its customer for tangible personal property that includes the amount paid to the supplier for the tangible personal property together with a markup, the advertising agency is the retailer of that tangible personal property and tax applies to that separately stated charge. If the advertising makes a lump sum charge to its client that includes the charge for the tangible~~

~~personal property as well as the charge for any nontaxable services or reproduction rights under subdivision (b), the advertising agency is the retailer of the tangible personal property provided and the measure of tax on the sale of that tangible personal property is calculated as provided in subdivision (b).~~

(d) TRANSFERS BY AN ARTIST AT A SOCIAL GATHERING. The transfer of original drawings, sketches, illustrations, or paintings by an artist at a social gathering for entertainment purposes is not a sale or use or purchase of tangible personal property, and the artist is the consumer of any property so transferred, when all the following requirements are satisfied:

- (1) Eighty percent or more of the drawings, sketches, illustrations, or paintings are delivered by the artist to a person or persons other than the purchaser;
- (2) Eighty percent or more of all of the drawings, sketches, illustrations, or paintings are received by a person or persons, other than the purchaser, at no cost to the person or persons who become the owner of the drawings, sketches, illustrations, or paintings;
- (3) The charge for the drawings, sketches, illustrations, or paintings is based on a preset fee; and
- (4) The preset fee charged for the drawings, sketches, illustrations, or paintings is contingent upon a minimum number of at least three drawings, sketches, illustrations, or paintings to be produced by the artist at the social gathering.

(e) CHARGES AND TRANSACTIONS GOVERNED BY OTHER REGULATIONS.

- (1) **AUDIO PRODUCTIONS.** Tax applies to charges for an audio production obtained or furnished by an advertising agency to its client as provided in Regulation 1527.
- (2) **PHOTOGRAPHY.** Tax applies to charges for photography as provided in Regulation 1528 except when the photographic image is furnished by a commercial artist as defined in subdivision (a)(3).
- (3) **TYPOGRAPHY.** Tax applies to charges for typography or composed type obtained from outside suppliers as provided in Regulation 1541.

(4) **VIDEO OR FILM PRODUCTIONS.** When a video or film production obtained or furnished by an advertising agency to its client constitutes qualified production services as defined in Regulation 1529, tax **does not apply** applies to the charges for such qualified production services as provided in Regulation 1529. **Similarly, tax does not apply to charges for creative art services or for qualified production services.**

Regulation 1540. ADVERTISING AGENCIES AND COMMERCIAL ARTISTS.

Reference: Sections 6006 - 6015, Revenue and Taxation Code.

(a) DEFINITIONS.

(1) ADVERTISING. Advertising is commercial communication utilizing one or more forms of communication (such as television, print, billboards, or the Internet) from or on behalf of an identified person to an intended target audience.

(2) ADVERTISING AGENCIES. Advertising agencies design and implement advertising campaigns for purposes of advertising the goods, services, or ideas of their clients. As part of that primary function, advertising agencies provide their clients with services (such as consultation, consumer research, media planning and placement, public relations, and other marketing activities) and tangible personal property (such as print advertisements, finished art, and video and audio productions).

(3) COMMERCIAL ARTISTS. Commercial artists, who may characterize themselves as commercial artists, commercial photographers, or designers, provide services and tangible personal property to their clients for use in their clients' advertising campaigns, or for their clients' other commercial endeavors such as sales of copies of finished art (including, e.g., photographic images) provided by a commercial artist. Services they provide to their clients include the creation and development of ideas, concepts, looks, or messages. Electronic artwork they provide may be transferred through remote telecommunications such as by modem or over the Internet, or by tangible means through electronic media such as compact or floppy disc. Tangible personal property they provide may include electronic media on which electronic artwork is transferred to the client, hard copies of the electronic artwork, hard copies of finished art (which may consist of photographic images).

(4) CONTRACT OF SALE. An agreement to transfer tangible personal property for consideration is a contract of sale. A contract of sale consists of all terms comprising the obligation of the parties for the sale and purchase of the tangible personal property in question. A contract of sale may consist of a single contract document. A contract of sale may also consist of multiple documents. For example, a master agreement between an advertising agency and its client may specify the obligations of each with respect to the design of an advertising campaign for the client, the placement of the advertising with print and television media, and for the sale and purchase of tangible personal property related to the advertising campaign. There may then be additional terms for the purchase of specific tangible personal property during the advertising campaign, such as in a purchase order, which identifies the specific property that will be purchased and sold and the sales price for that property. In this example, not all terms of the sale and purchase of the tangible personal property identified in the purchase order are included in the master agreement, nor are all terms included in the purchase order. Rather, the contract of sale in this circumstance consists of the relevant provisions of the master agreement as modified by the specific provisions in the purchase order.

(5) DIGITAL PRE-PRESS INSTRUCTION. Digital pre-press instruction is the creation of original information in electronic form by combining more than one computer program into specific instructions or information necessary to prepare and link files for electronic transmission for output to film, plate, or direct to press, which is then transferred on electronic media such as tape or compact disc.

(6) ELECTRONIC ARTWORK. Electronic artwork is artwork created through the use of computer hardware and software processes which results in artwork in a digital format that can be transmitted to others via electronic means (that is, transmitted through remote telecommunications such as by modem or over the Internet, or by electronic media such as compact or floppy disc). Elements of the process include the creation of original artwork or photographic images, scanning of artwork or photographic images, composition and design of text, insertion and manipulation of scanned and original electronic artwork, photographic images, and text. Electronic artwork does not include artwork that is transferred to clients in a tangible form, other than on electronic media, even where such artwork may have been manufactured or produced in whole or in part by computer hardware and software processes.

(7) FINISHED ART. Finished art is the final artwork used for actual reproduction by photomechanical or other processes, or used for display. It includes electronic artwork, illustrations (e.g. drawings, diagrams, halftones, or color images), photographic images, sculptures, paintings, and handlettering. Blueprints, diagrams, and instructions for signage furnished to a client as the result of environmental graphic design services are not finished art.

(8) HARD COPIES. An item is transferred on hard copy when it is transferred on any tangible personal property other than in digital format on electronic media. For example, finished art transferred on canvas or paper is transferred on hard copy while a transfer of finished art in digital format on compact or floppy disc is not regarded as a transfer on hard copy.

(9) INTERMEDIATE PRODUCTION AIDS. Intermediate production aids include items such as artwork, illustrations, photograph images, photo engravings, and other similar materials which are used to produce special printing aids or other intermediate production aids.

(10) MASTER AGREEMENT. A master agreement is a contract, however characterized (such as "agency-client agreement"), entered into between an advertising agency or commercial artist and its client which specifies the obligations of each party to the master agreement with respect to their relationship, whether for a specified time or advertising campaign or until one of the parties terminates the agreement. After entering into a master agreement, the parties may thereafter enter into additional contracts, including fulfillment of purchase orders issued by the client for the purchase of specific services, tangible personal property, or both, which additional contracts include all the terms in the master agreement which are not explicitly in conflict with the later contracts.

(11) PRELIMINARY ART. Preliminary art is tangible personal property which is prepared solely for the purpose of demonstrating an idea or message for acceptance by the client before a contract is entered into or before approval is given for preparation of finished art to be furnished or licensed by the seller to his or her client, provided neither title to nor permanent possession of such tangible personal property passes to the client. Preliminary art may include roughs, visualizations, layouts, comprehensives, and instant photos.

(12) SPECIAL PRINTING AIDS. Special printing aids are reusable manufacturing aids which are used by a printer during the printing process and are of unique utility to a particular client. Special printing aids include electrotypes, stereotypes, photoengravings, silk screens, steel dies, cutting dies, lithographic plates, film, single or multi color separation negatives, and flats.

(13) THIRD PARTIES. A reference in this regulation to a transfer to a client also includes a transfer to a third party on the client's behalf. For example, the discussion in subdivision (b)(2)(B) for transfers of finished art by loading into the client's computer also includes transfers of the finished art by loading it into a third party's computer at the instruction of the client.

(b) APPLICATION OF TAX TO ACTIVITIES OF ADVERTISING AGENCIES AND COMMERCIAL ARTISTS.

(1) SERVICES.

(A) General.

1. Services performed to convey ideas, concepts, looks, or messages to a client may result in a transfer, enhancement, or revision of either electronic artwork, hard copies of electronic artwork, or copies of manually prepared artwork. If charges for such services are separately stated as "design charges," "preliminary art," "concept development," or any other designation that clearly indicates that the charges are for such services and not for finished art, they are nontaxable unless the master agreement or other contract provides that the advertising agency or commercial artist will pass to the client title or the right to permanent possession of the artwork in tangible form, such as on electronic media or hard copy, or permanent possession of the artwork in tangible form is, in fact, transferred to the client. However, if the master agreement provides that the client owns the concepts embodied in tangible personal property that is owned and possessed by the advertising agency or commercial artist (e.g., so that such concepts cannot be used on behalf of any other person), that contract provision does not constitute the passage of title to tangible personal property to the client, provided the client does not thereby obtain the actual title to, or permanent possession of, the tangible personal property embodying the concepts and no other contractual provision passes such title to, or permanent possession of, such tangible personal property. A requirement that an advertising agency or commercial artist retain permanent possession of the artwork in tangible form does not itself constitute a sale of that property to the client in the absence of a provision passing title to such property to the client.

2. Tangible personal property developed and used during services performed to convey ideas, concepts, looks, or messages is consumed in the performance of those services. Unless, prior to any use, the advertising agency or commercial artist passes title to such property to the client as discussed in the previous paragraph, the advertising agency or commercial artist is the consumer of such tangible personal property used and tax applies to the sale of property to, or to the use of the property by, the advertising agency or commercial artist. If the advertising agency or commercial artist passes title to, or permanent possession of, such tangible personal property to its client, tax applies to the sale of the tangible personal property by the advertising agency or commercial artist to the client.

(B) Digital Pre-Press Instruction. Digital pre-press instruction is a custom computer program under section 6010.9 of the Revenue and Taxation Code, the sale of which is not subject to tax, provided the digital pre-press instruction is prepared to the special order of the purchaser. Digital pre-press instruction shall not, however, be regarded as a custom computer program if it is a “canned” or prewritten computer program which is held or existing for general or repeated sale or lease, even if the digital pre-press instruction was initially developed on a custom basis or for in-house use. The sale of such canned or prewritten digital pre-press instruction in tangible form is a sale of tangible personal property, the retail sale of which is subject to tax.

(C) Retouching Photographic Images. Retouching a photographic image for the purpose of repairing or restoring the photograph to its original condition is a repair, the charge for which is not taxable.

(D) Signage. The creation and providing of single copies of blueprints, diagrams, and instructions for signage as a result of environmental graphic design is a service the charge for which is not taxable. Charges for additional copies are taxable.

(E) Websites. The design, editing, or hosting of an electronic website in which no tangible personal property is transferred to the client is a service, the charge for which is not subject to tax.

(F) Specific Nontaxable Charges. The following and similar fees and commissions are not taxable when they are separately stated. Whether separately stated or not, these fees and commissions are not included in the calculation of “direct labor” for purposes of subdivision (b)(3).

1. Media commissions received for placement of advertising whether paid by the medium, by another advertising agency, or by the client.

2. Commissions paid to advertising agencies by suppliers. Examples of such commissions are those paid to an advertising agency by a premium manufacturer (or distributor) or a direct-by-mail supplier.

3. Consultation and concept development fees related to client discussion, development of ideas, and other services. If the advertising agency transfers to the client tangible personal property produced as a result of these services, the transfer is incidental to the advertising agency's providing of the service and is not a sale of that tangible personal property; the advertising agency is the consumer of tangible personal property transferred to the client incidental to the providing of a service.

4. Fees for research or account planning that entail consumer research and the application of that research to the client's business or industry.

5. Fees for quality control supervision that entails the proofing and review of printing and other products provided by outside suppliers.

6. Charges for the formulation and writing of copy.

(G) Example. A designer contracts to create and sell printed brochures to a law firm. The contract separately states a charge for design, for art direction, for preliminary art, and for the printed brochures. The designer's design and art direction services culminate in the creation of preliminary art that the designer uses to show the designer's concepts to the law firm. After the law firm approves the concepts, the designer finalizes the design of the brochure and contracts with a printer to print the brochures. The printer sells the printed brochures to the designer for resale, and the designer resells the printed brochures to the law firm. The only tangible personal property that will be transferred to the law firm (or to anyone on behalf of the law firm) are the printed brochures. The law firm will not obtain title to, or the right to possession of, any finished art or any other tangible personal property. Tax does not apply to the designer's separately stated charges for design, art direction, and preliminary art. Tax applies to the designer's separately stated charge to the law firm for the printed brochures.

(2) FINISHED ART.

(A) Use of Aids in Creation of Finished Art. If the advertising agency or commercial artist uses any intermediate production aids or special printing aids in the creation of the finished art, the presumptions with respect to passage of title and the calculation of the measure of tax on the sale of such aids by the advertising agency or commercial artist, is governed by the provisions of Regulation 1541 applicable to special printing aids.

(B) Transfers of Finished Art Not in Tangible Form. A transfer of electronic artwork from an advertising agency or commercial artist to the client or to a third party on the client's behalf that is not in tangible form is not a sale of tangible personal property, and the charges for the transfer are not subject to tax. A transfer of electronic artwork is not in tangible form if the file containing the electronic artwork is transferred through remote telecommunications (such as by modem or over the Internet), or if the file is loaded into the client's computer by the advertising agency or commercial artist, and the client does not obtain title to or possession of any tangible personal property, such as electronic media or hard copy. If the transfer is not a transfer in

tangible form because it is loaded onto the client's computer, the advertising agency or commercial artist should document that transfer by a written statement signed at the time of loading by the client and by the person who loaded the electronic artwork into the client's computer with the following or similar language: "This electronic artwork was loaded into the computer of [client's name] by [seller's name], and [seller's name] did not transfer any tangible personal property containing the artwork, such as electronic media or hard copies, to [client's name]." When such a statement is signed at the time the file is loaded, it will be rebuttably presumed that the transfer of electronic artwork was not transferred in tangible form. If there is no such timely completed statement, the advertising agency or commercial artist may provide other substantive evidence establishing that the artwork was not transferred in tangible form.

(C) Transfers of Finished Art in Tangible Form. The electronic or manual preparation of finished art for use in reproduction or display is not a service. Unless the transfer is not in tangible form as explained in subdivision (b)(2)(B), the transfer of finished art is a sale of tangible personal property and tax applies to charges for that finished art, including all charges for any rights sold with the finished art, such as copyrights or distribution and production rights, except as provided in subdivision (b)(2)(D)2. If charges for finished art are combined into a single charge that also includes nontaxable charges for conceptual services described in subdivision (b)(1)(A), the advertising agency or commercial artist may report the measure of tax on the retail sale of the finished art as specified in subdivision (b)(3), provided that the reported measure of tax must also include the value of reproduction rights included with the transfer except those that are not taxable as provided in subdivision (b)(2)(D)2. If tax is not reported on this basis, it will be rebuttably presumed that 75 percent of the combined charge for the finished art and conceptual services is for the nontaxable services and that 25 percent of the combined charge is the measure of tax on the retail sale of the finished art, provided that 25 percent of the combined charge is not less than the sales price to the advertising agency or commercial artist of the finished art (or component parts) and any intermediate production aids or special printing aids sold to the client for that combined charge. If such sales price to the advertising agency or commercial artist is more than 25 percent of the combined charge to the client, the measure of tax shall be deemed to be such sales price of the tangible personal property to the advertising agency or commercial artist.

(D) Reproduction Rights Transferred With Finished Art.

1. Charges for the transfer of possession in tangible form to the client or to anyone else on the client's behalf of finished art for purposes of reproduction are included in the measure of tax on that sale, including all charges for the right to use that property, even though there is no transfer of title to the person reproducing the finished art, except as provided in subdivision (b)(2)(D)2.

2. Any agreement evidenced by a writing (such as a contract, invoice, or purchase order) that assigns or licenses a copyright interest in finished art for the purpose of reproducing and selling other property subject to the copyright interest is a technology transfer agreement, as explained further in Regulation 1507. Tax applies to amounts received for any tangible personal

property transferred as part of a technology transfer agreement. Tax does not apply to amounts received for the assignment or licensing of a copyright interest as part of a technology transfer agreement. The measure of tax on the sale of finished art transferred by an advertising agency or commercial artist as part of a technology transfer agreement shall be:

a. The separately stated sales price for the finished art, provided the separately stated price represents a fair market value of the tangible personal property;

b. Where there is no such separately stated price, the separate price at which the person holding the copyright interest in the finished art has sold or leased that finished art or like finished art to an unrelated third party where: 1) the finished art was sold or leased without also transferring an interest in the copyright; or 2) the finished art was sold or leased in another transaction at a stated price satisfying the requirements of subdivisions (b)(2)(D)2.a.; or

c. If there is no such separately stated price under subdivision (b)(2)(D)2.a., nor a separate price under subdivision (b)(2)(D)2.b., 200 percent of the combined cost of materials and labor used to produce or acquire the finished art. "Cost of materials" consists of the costs of those materials used or incorporated into the finished art, or any tangible personal property transferred as part of the technology transfer agreement. "Labor" includes any charges or value of labor used to create such tangible personal property whether the advertising agency or commercial artist performs such labor, a third party performs the labor, or the labor is performed through some combination thereof. The value of labor provided by the advertising agency or commercial artist shall equal the lower of the normal and customary charges for labor billed to third parties by the advertising agency or commercial artist, or the fair market value of the labor performed by the advertising agency or commercial artist.

(3) SALES OF OTHER TANGIBLE PERSONAL PROPERTY BY ADVERTISING AGENCY OR COMMERCIAL ARTIST. Tax applies to the total charge for the retail sale of tangible personal property by an advertising agency or commercial artist. If an advertising agency or commercial artist combines charges for nontaxable services as defined in subdivision (b)(1)(F), such as media placement, with charges for tangible personal property for which the advertising agency or commercial artist is the retailer, the measure of tax on that retail sale of property includes the total of: direct labor; the cost of purchased items that become an ingredient or component part of the tangible personal property; the cost of any intermediate production aids or special printing aids; and a reasonable markup. Commissions, fees, and other charges exclusively related to the production or fabrication of tangible personal property are part of direct labor and are thus included in the measure of tax. Such charges include retouching of photographic images or other artwork for reproduction, provided the retouching is intended to improve the quality of the reproduction. An advertising agency or commercial artist must keep sufficient records to document the basis for the reported measure of tax.

(4) ITEMS PURCHASED BY AN ADVERTISING AGENCY OR COMMERCIAL ARTIST. Except when property is resold prior to any use, an advertising agency or commercial artist is the consumer of tangible personal property used in the operation of its business. Tax applies to the

sale of such property to, or to the use of such property by, the advertising agency or commercial artist.

(c) SITUATIONS SPECIFIC TO ADVERTISING AGENCIES.

(1) ADVERTISING AGENCY ACTING AS AN AGENT FOR ITS CLIENT. An agent is one who represents another, called the principal, in dealings with third persons. (Civil Code section 2295.) To the extent that an advertising agency acts as the agent of its client when acquiring tangible personal property, it is neither a purchaser of the property with respect to the supplier nor a seller of the property with respect to its principal (that is, its client). Because of the unique relationship between advertising agencies and their clients, unless an advertising agency elects non-agent status under subdivision (c)(2)(A) or is otherwise the retailer of the property under subdivision (c)(2)(B) or (c)(2)(C), it is rebuttably presumed that the advertising agency acts as the agent of its client when acquiring tangible personal property on its client's behalf.

(A) A supplier of tangible personal property to an advertising agency is presumed to have made a retail sale of that property unless the supplier takes a timely and valid resale certificate in good faith from the advertising agency. Otherwise, the supplier has the burden of establishing that the advertising agency elected non-agent status under subdivision (c)(2)(A) and resold the property or that the advertising agency resold the property as the retailer under subdivision (c)(2)(B) or (c)(2)(C).

(B) When an advertising agency is the agent of its client for the purchase of tangible personal property under subdivision (c)(1), sales or use tax is due on the purchase price from the supplier to the advertising agency. Tax does not apply to the charge made by an advertising agency to its client for reimbursement, including tax reimbursement, for the amount charged by a supplier, nor does tax apply to the advertising agency's separately stated charges for its services directly related to its acquisition of such tangible personal property (e.g., when the advertising agency makes a separately itemized charge for reimbursement of the amount paid to the supplier of the property, tax does not apply to a separately itemized "agency fee"). When the applicable tax is use tax and the advertising agency does not pay that use tax to the supplier on the client's behalf, the advertising agency is liable for the use tax and must report and pay the use tax to the Board. The advertising agency's liability for that use tax is not extinguished unless the client has self-reported and paid the tax to the Board.

(C) An advertising agency may not issue a resale certificate when purchasing tangible personal property as the agent of its client. An advertising agency who issues a resale certificate to a supplier is presumed to be purchasing tangible personal property from that supplier on its own behalf for resale and not to be acting as an agent of its client. However, the advertising agency may provide evidence to prove that its issuance of the resale certificate was erroneous and that the advertising agency was acting as an agent of its client, provided the advertising agency has not treated the transaction as its own sale of tangible personal property to its client, collecting tax or tax reimbursement from its client on that sale. If the resale certificate was issued in error, the advertising agency is liable for use tax on the cost of tangible personal

property purchased under the certificate unless the advertising agency has already paid that tax to the supplier or to the Board, or the client has self-reported and paid the tax to the Board.

(2) ADVERTISING AGENCY ACTING AS A RETAILER. An advertising agency that acts as a retailer of tangible personal property may issue a resale certificate for such tangible personal property if the property will be resold prior to any use. Absent an agreement that the property will be sold prior to use, tax is due on the purchase price of tangible personal property that is used prior to being resold to the client and, in addition, tax is also due on the sales price of the tangible personal property to the client.

(A) Election of Non-Agent Status. An advertising agency may elect non-agent status with respect to sales of tangible personal property to its client. This election must be supported by a specific written statement in its master agreement with the client. Alternatively, a statement may be included on an advertising agency's job order or invoice to its client. Statements should include the following or similar language: "(Advertising Agency's name) will not be acting as an agent of (client's name) for purposes of this transaction."

An advertising agency that elects non-agent status is a retailer with respect to tangible personal property sold to its clients. The measure of tax on the advertising agency's retail sale is the separately stated charge for the tangible personal property. If there is no such separately stated charge, the measure of tax is calculated as provided in subdivision (b).

(B) Items Produced or Fabricated by an Advertising Agency In-House. Advertising agencies are retailers of tangible personal property they produce or fabricate, e.g., by their own employees. Advertising agencies are not agents of their clients with respect to the acquisition of materials incorporated into such items of tangible personal property they produce or fabricate, but instead are the retailers of such property. The measure of tax on their retail sale of that property is the separately stated charge for the property sold. If there is no such separately stated charge, the measure of tax is calculated as provided in subdivision (b).

(C) Invoice to Client for More Than Cost of Tangible Personal Property to Advertising Agency. When an advertising agency invoices its client for tangible personal property provided by the advertising agency without separately stating the amount paid to the supplier for that property, the advertising agency is the retailer of the tangible personal property to its client. For example, when the advertising agency invoices a single charge to its client for tangible personal property that includes the amount paid to the supplier for the tangible personal property together with a markup, the advertising agency is the retailer of that tangible personal property and tax applies to that separately stated charge. If the advertising agency makes a lump sum charge to its client that includes the charge for the tangible personal property as well as the charge for any nontaxable services or reproduction rights under subdivision (b), the advertising agency is the retailer of the tangible personal property provided and the measure of tax on the sale of that tangible personal property is calculated as provided in subdivision (b).

(d) TRANSFERS BY AN ARTIST AT A SOCIAL GATHERING. The transfer of original drawings, sketches, illustrations, or paintings by an artist at a social gathering for entertainment purposes is not a sale or use or purchase of tangible personal property, and the artist is the consumer of any property so transferred, when all the following requirements are satisfied:

(1) Eighty percent or more of the drawings, sketches, illustrations, or paintings are delivered by the artist to a person or persons other than the purchaser;

(2) Eighty percent or more of all of the drawings, sketches, illustrations, or paintings are received by a person or persons, other than the purchaser, at no cost to the person or persons who become the owner of the drawings, sketches, illustrations, or paintings;

(3) The charge for the drawings, sketches, illustrations, or paintings is based on a preset fee; and

(4) The preset fee charged for the drawings, sketches, illustrations, or paintings is contingent upon a minimum number of at least three drawings, sketches, illustrations, or paintings to be produced by the artist at the social gathering.

(e) CHARGES AND TRANSACTIONS GOVERNED BY OTHER REGULATIONS.

(1) AUDIO PRODUCTIONS. Tax applies to charges for an audio production obtained or furnished by an advertising agency to its client as provided in Regulation 1527.

(2) PHOTOGRAPHY. Tax applies to charges for photography as provided in Regulation 1528 except when the photographic image is furnished by a commercial artist as defined in subdivision (a)(3).

(3) PRINTED SALES MESSAGES. Qualifying sales of printed sales messages may qualify for exemption, as explained in Regulation 1541.5.

(4) TYPOGRAPHY. Tax applies to charges for typography or composed type obtained from outside suppliers as provided in Regulation 1541.

(5) VIDEO OR FILM PRODUCTIONS. When a video or film production obtained or furnished by an advertising agency to its client constitutes qualified production services as defined in Regulation 1529, tax applies to the charges for such qualified production services as provided in Regulation 1529.

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Action 2- Special Printing Aids	<p>Regulation 1541. PRINTING AND RELATED ARTS.</p> <p>(c) SPECIAL PRINTING AIDS. In General. In recognition of the unique utility that special printing aids have to the sale of printed material, and the need to avoid burdening businesses with unnecessary paperwork, the following presumptions shall apply.</p> <p>(1) With respect to sales of printed material ultimately subject to sales tax, or sales to the U. S. Government, it shall be presumed that the selling price of the printed material includes the selling price of the special printing aids and that title passed to the customer, irrespective of whether or not the printer separately itemizes the special printing aids. It shall be further presumed that the printer, or other reseller, discussed in the following paragraph, made no use of the special printing aids prior to their sale. Accordingly the printer may purchase the special printing aids for resale.</p>	<p>Regulation 1541. PRINTING AND RELATED ARTS.</p> <p>(c) SPECIAL PRINTING AIDS. In General. In recognition of the unique utility that special printing aids have to the sale of printed material, and the need to avoid burdening businesses with unnecessary paperwork, the following presumptions shall apply.</p> <p>(1) With respect to sales of printed material ultimately subject to sales tax, or sales to the U. S. Government, it shall be presumed that the selling price of the printed material includes the selling price of the special printing aids and that title passed to the customer, irrespective of whether or not the printer separately itemizes the special printing aids. It shall be further presumed that the printer, or other reseller, discussed in the following paragraph, made no use of the special printing aids prior to their sale. Accordingly the printer may purchase the special printing aids for resale.</p>	<p>Regulation 1541. PRINTING AND RELATED ARTS.</p> <p>(OPTION 1)</p> <p>(c) SPECIAL PRINTING AIDS. In General. In recognition of the unique utility that special printing aids have to the sale of printed material, and the need to avoid burdening businesses with unnecessary paperwork, the following presumptions shall apply.</p> <p>(1) With respect to sales of printed material ultimately subject to sales tax, or sales to the U. S. Government, it shall be presumed that the selling price of the printed material includes the selling price of the special printing aids and that title passed to the customer, irrespective of whether or not the printer separately itemizes the special printing aids. It shall be further presumed that the printer, or other reseller, discussed in the following paragraph, made no use of the special printing aids prior to their sale. Accordingly the printer may purchase the special printing aids for resale.</p>	<p>Mr. Patrick Leone proposes to keep the original language for subdivision (c) on special printing aids. [Option 1]</p> <p>However, if staff's proposed language is adopted, Mr. Leone proposes that the language requiring printers to separately state the printing aids on their sales invoice be on a prospective basis. (See page 6.) [Option 2]</p>

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	<p>“Ultimately subject to sales tax,” means either the printer's sale of the printed material and special printing aids is subject to sales tax or is an exempt sale to the U. S. Government, or if the printer's sale of the printed material is for resale, a subsequent sale of the printed material and special printing aids is subject to California sales tax or is an exempt sale to the U. S. Government.</p> <p>When the printer's sale of printed material is a sale for resale, as described in the above paragraph, unless the printer timely takes a valid resale certificate in good faith that states the special printing aids are to be purchased for resale, tax is due on the selling price of the special printing aids whether or not the selling price is separately itemized. The selling price of the special printing aids is deemed to be the sales price of the special printing aids, or their components, to the printer regardless of the amount of the separately stated charge, if any, for the special printing aid. The printer need not separately charge sales tax reimbursement to their customer and if the printer has paid sales or use tax on the selling price of the special printing aids or their components to the printer, no additional tax is due.</p>	<p>“Ultimately subject to sales tax,” means either the printer's sale of the printed material and special printing aids is subject to sales tax or is an exempt sale to the U. S. Government, or if the printer's sale of the printed material is for resale, a subsequent sale of the printed material and special printing aids is subject to California sales tax or is an exempt sale to the U. S. Government.</p> <p>When the printer's sale of printed material is a sale for resale, as described in the above paragraph, unless the printer timely takes a valid resale certificate in good faith that states the special printing aids are to be purchased for resale, tax is due on the selling price of the special printing aids whether or not the selling price is separately itemized. The selling price of the special printing aids is deemed to be the sales price of the special printing aids, or their components, to the printer regardless of the amount of the separately stated charge, if any, for the special printing aid. The printer need not separately charge sales tax reimbursement to their customer and if the printer has paid sales or use tax on the selling price of the special printing aids or their components to the printer, no additional tax is due.</p>	<p>“Ultimately subject to sales tax,” means either the printer's sale of the printed material and special printing aids is subject to sales tax or is an exempt sale to the U. S. Government, or if the printer's sale of the printed material is for resale, a subsequent sale of the printed material and special printing aids is subject to California sales tax or is an exempt sale to the U. S. Government.</p> <p>When the printer's sale of printed material is a sale for resale, as described in the above paragraph, unless the printer timely takes a valid resale certificate in good faith that states the special printing aids are to be purchased for resale, tax is due on the selling price of the special printing aids whether or not the selling price is separately itemized. The selling price of the special printing aids is deemed to be the sales price of the special printing aids, or their components, to the printer regardless of the amount of the separately stated charge, if any, for the special printing aid. The printer need not separately charge sales tax reimbursement to their customer and if the printer has paid sales or use tax on the selling price of the special printing aids or their components to the printer, no additional tax is due.</p>	

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	<p>The term “special printing aids” on a resale certificate shall be sufficient to cover all special printing aids as defined in subdivision (a)(1).</p> <p>(2) If a printer does not wish to sell special printing aids in connection with the sale of printed material ultimately subject to sales tax or sold to the U. S. Government, described in (c)(1) above, the following statement should be included on the sales invoice: “The selling price of the printed material does not include the transfer of title to the special printing aids.” The printer would then be the owner and consumer of the special printing aids. Tax would apply to both the retail sale of the printed material and the cost to the printer of the special printing aids.</p> <p>(3) With respect to all other sales of printed material, as for example, sales in interstate commerce, sales of exempt newspapers or periodicals, or sales of exempt printed sales messages, it shall also be presumed that the selling price of the printed material includes the selling price of the special printing aids and that title passed to the customer irrespective of whether or not the printer separately itemizes the special printing aids. It shall be further presumed that the printer made no use</p>	<p>The term “special printing aids” on a resale certificate shall be sufficient to cover all special printing aids as defined in subdivision (a)(1).</p> <p>—(2) If a printer does not wish to sell special printing aids in connection with the sale of printed material ultimately subject to sales tax or sold to the U. S. Government, described in (c)(1) above, the following statement should be included on the sales invoice: “The selling price of the printed material does not include the transfer of title to the special printing aids.” The printer would then be the owner and consumer of the special printing aids. Tax would apply to both the retail sale of the printed material and the cost to the printer of the special printing aids.</p> <p>—(3) With respect to all other sales of printed material, as for example, sales in interstate commerce, sales of exempt newspapers or periodicals, or sales of exempt printed sales messages, it shall also be presumed that the selling price of the printed material includes the selling price of the special printing aids and that title passed to the customer irrespective of whether or not the printer separately itemizes the special printing aids. It shall be further presumed that the printer made no use</p>	<p>The term “special printing aids” on a resale certificate shall be sufficient to cover all special printing aids as defined in subdivision (a)(1).</p> <p>(2) If a printer does not wish to sell special printing aids in connection with the sale of printed material ultimately subject to sales tax or sold to the U. S. Government, described in (c)(1) above, the following statement should be included on the sales invoice: “The selling price of the printed material does not include the transfer of title to the special printing aids.” The printer would then be the owner and consumer of the special printing aids. Tax would apply to both the retail sale of the printed material and the cost to the printer of the special printing aids.</p> <p>(3) With respect to all other sales of printed material, as for example, sales in interstate commerce, sales of exempt newspapers or periodicals, or sales of exempt printed sales messages, it shall also be presumed that the selling price of the printed material includes the selling price of the special printing aids and that title passed to the customer irrespective of whether or not the printer separately itemizes the special printing aids. It shall be further presumed that the printer made no use</p>	

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	<p>of the special printing aids prior to their sale. Sales tax is due on the selling price of the special printing aids whether or not the selling price of the special printing aids is separately stated. The selling price of the special printing aids is deemed to be the sales price of the special printing aids, or their components, to the printer regardless of the amount of the separately stated charge, if any, for the special printing aid.</p> <p>The printer need not separately charge sales tax reimbursement to their customer and if the printer has paid sales or use tax on the selling price of the special printing aids or their components to the printer, no additional tax is due.</p> <p>However, sales tax is not due on the selling price of the special printing aids discussed in (c)(3) if the printer timely takes a valid resale certificate in good faith that states the special printing aids are to be purchased for resale. The term "special printing aids" on a resale certificate shall be sufficient to cover all special printing aids as defined in subdivision (a)(1).</p> <p>Persons issuing resale certificates for special printing aids as discussed in</p>	<p>of the special printing aids prior to their sale. Sales tax is due on the selling price of the special printing aids whether or not the selling price of the special printing aids is separately stated. The selling price of the special printing aids is deemed to be the sales price of the special printing aids, or their components, to the printer regardless of the amount of the separately stated charge, if any, for the special printing aid.</p> <p>The printer need not separately charge sales tax reimbursement to their customer and if the printer has paid sales or use tax on the selling price of the special printing aids or their components to the printer, no additional tax is due.</p> <p>However, sales tax is not due on the selling price of the special printing aids discussed in (c)(3) if the printer timely takes a valid resale certificate in good faith that states the special printing aids are to be purchased for resale. The term "special printing aids" on a resale certificate shall be sufficient to cover all special printing aids as defined in subdivision (a)(1).</p> <p>Persons issuing resale certificates for special printing aids as discussed in</p>	<p>of the special printing aids prior to their sale. Sales tax is due on the selling price of the special printing aids whether or not the selling price of the special printing aids is separately stated. The selling price of the special printing aids is deemed to be the sales price of the special printing aids, or their components, to the printer regardless of the amount of the separately stated charge, if any, for the special printing aid.</p> <p>The printer need not separately charge sales tax reimbursement to their customer and if the printer has paid sales or use tax on the selling price of the special printing aids or their components to the printer, no additional tax is due.</p> <p>However, sales tax is not due on the selling price of the special printing aids discussed in (c)(3) if the printer timely takes a valid resale certificate in good faith that states the special printing aids are to be purchased for resale. The term "special printing aids" on a resale certificate shall be sufficient to cover all special printing aids as defined in subdivision (a)(1).</p> <p>Persons issuing resale certificates for special printing aids as discussed in</p>	

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	<p>(c)(3) are then liable for the tax on their selling price of the special printing aids irrespective of whether or not the printer separately itemized the printing aids to the person issuing the resale certificate and notwithstanding that the printed material is exempt from tax as for example, a sale in interstate commerce, a sale of exempt newspapers or periodicals or a sale of exempt printed sales messages. In no event shall the selling price of the special printing aids be less than the selling price of the special printing aids, or their components, to the printer.</p> <p>If the printer's sale includes both a sale of printed material ultimately subject to sales tax, as described in (c)(1) above, and a sale of printed material as described in (c)(3) ("split sale"), tax is due on the selling price of the special printing aids. Absent a separate itemization, as long as tax is reported on an amount equal to at least the selling price of the special printing aids or their components to the printer, no further tax will be due on the selling price of the special printing aids.</p> <p>(4) If a printer does not wish to sell special printing aids in connection with all other sales of printed material, as</p>	<p>(c)(3) are then liable for the tax on their selling price of the special printing aids irrespective of whether or not the printer separately itemized the printing aids to the person issuing the resale certificate and notwithstanding that the printed material is exempt from tax as for example, a sale in interstate commerce, a sale of exempt newspapers or periodicals or a sale of exempt printed sales messages. In no event shall the selling price of the special printing aids be less than the selling price of the special printing aids, or their components, to the printer.</p> <p>If the printer's sale includes both a sale of printed material ultimately subject to sales tax, as described in (c)(1) above, and a sale of printed material as described in (c)(3) ("split sale"), tax is due on the selling price of the special printing aids. Absent a separate itemization, as long as tax is reported on an amount equal to at least the selling price of the special printing aids or their components to the printer, no further tax will be due on the selling price of the special printing aids.</p> <p>(4) If a printer does not wish to sell special printing aids in connection with all other sales of printed material, as</p>	<p>(c)(3) are then liable for the tax on their selling price of the special printing aids irrespective of whether or not the printer separately itemized the printing aids to the person issuing the resale certificate and notwithstanding that the printed material is exempt from tax as for example, a sale in interstate commerce, a sale of exempt newspapers or periodicals or a sale of exempt printed sales messages. In no event shall the selling price of the special printing aids be less than the selling price of the special printing aids, or their components, to the printer.</p> <p>If the printer's sale includes both a sale of printed material ultimately subject to sales tax, as described in (c)(1) above, and a sale of printed material as described in (c)(3) ("split sale"), tax is due on the selling price of the special printing aids. Absent a separate itemization, as long as tax is reported on an amount equal to at least the selling price of the special printing aids or their components to the printer, no further tax will be due on the selling price of the special printing aids.</p> <p>(4) If a printer does not wish to sell special printing aids in connection with all other sales of printed material, as</p>	

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	<p>discussed in (c)(3) above, the following statement should be included on the sales invoice: "The selling price of the printed material does not include the transfer of title to the special printing aids." The printer would then be the owner and consumer of the special printing aids. Tax would apply to the cost to the printer of the special printing aids.</p> <p>(5) No other proof shall be required with respect to passage of title on special printing aids.</p>	<p>discussed in (c)(3) above, the following statement should be included on the sales invoice: "The selling price of the printed material does not include the transfer of title to the special printing aids." The printer would then be the owner and consumer of the special printing aids. Tax would apply to the cost to the printer of the special printing aids.</p> <p>-(5) No other proof shall be required with respect to passage of title on special printing aids.</p> <p><u>(c) SPECIAL PRINTING AIDS. In recognition of the unique utility that special printing aids have to the production of printed matter, the practices of the industry, and the need to avoid burdening businesses with unnecessary paperwork, the presumptions and rules set forth in this subdivision apply to a printer's purchase and sale of special printing aids used to produce printed matter sold by the printer.</u></p> <p><u>(2) PRINTER'S SALE OF SPECIAL PRINTING AIDS. When the printer is regarded as purchasing the special</u></p>	<p>discussed in (c)(3) above, the following statement should be included on the sales invoice: "The selling price of the printed material does not include the transfer of title to the special printing aids." The printer would then be the owner and consumer of the special printing aids. Tax would apply to the cost to the printer of the special printing aids.</p> <p>(5) No other proof shall be required with respect to passage of title on special printing aids.</p> <p>OPTION 2</p> <p><u>(c) SPECIAL PRINTING AIDS. In recognition of the unique utility that special printing aids have to the production of printed matter, the practices of the industry, and the need to avoid burdening businesses with unnecessary paperwork, the presumptions and rules set forth in this subdivision apply to a printer's purchase and sale of special printing aids used to produce printed matter sold by the printer.</u></p> <p><u>(2) PRINTER'S SALE OF SPECIAL PRINTING AIDS. When the printer is regarded as purchasing the special</u></p>	<p>If staff's proposed language is adopted, Mr. Leone proposes that the language requiring printers to separately state the printing aids on their sales invoice be operative October 1, 2002, as noted in</p>

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		<p><u>printing aids for resale under subdivision (c)(1)(B), the following rules apply to determine the application of tax to the printer's sale of those special printing aids along with the printed matter produced with the special printing aids.</u></p> <p><u>(B) Nontaxable Sales of Special Printing Aids for Resale.</u> A person purchasing printed matter for resale may also purchase the special printing aids used to produce the printed matter for resale if that person will, in fact, resell the special printing aids prior to any use. A printer will not be regarded as selling special printing aids for resale unless: 1) the printer separately states the sale price of the special printing aids in an amount not less than the sale price of the special printing aids, or their components, to the printer; and 2) the printer accepts a timely and valid resale certificate in good faith from the printer's customer stating that the special printing aids are purchased for resale. The term "special printing aids" on a resale certificate shall be sufficient to cover all special printing aids as defined in subdivision (a)(12), and a printer accepting such a</p>	<p><u>printing aids for resale under subdivision (c)(1)(B), the following rules apply to determine the application of tax to the printer's sale of those special printing aids along with the printed matter produced with the special printing aids.</u></p> <p><u>(B) Nontaxable Sales of Special Printing Aids for Resale.</u> A person purchasing printed matter for resale may also purchase the special printing aids used to produce the printed matter for resale if that person will, in fact, resell the special printing aids prior to any use. A printer will not be regarded as selling special printing aids for resale unless: 1) operative October 1, 2002, the printer separately states the sale price of the special printing aids in an amount not less than the sale price of the special printing aids, or their components, to the printer; and 2) the printer accepts a timely and valid resale certificate in good faith from the printer's customer stating that the special printing aids are purchased for resale. The term "special printing aids" on a resale certificate shall be sufficient to cover all special printing aids as defined in subdivision (a)(12), and a</p>	<p>subdivision (c)(2)(B) and (c)(2)(B)(1).</p> <p>Mr. Leone believes staff's proposal is a change in the current application of tax.</p> <p>Staff believes that replacing the terminology "ultimately subject to tax" does not change the application of tax or the meaning of the regulation. In addition, this terminology is technically incorrect in that it refers to transactions which are not, in fact, subject to</p>

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		<p><u>resale certificate in good faith will be regarded as selling the special printing aids for resale provided the printer includes the required separately stated price for them. Otherwise, the printer will be regarded as selling the special printing aids at retail, and will owe tax on that retail sale accordingly. A printer might sell special printing aids for resale along with printed matter under circumstances where the sale of the printed matter is for resale and also qualifies for exemption, such as a sale in interstate commerce where the purchaser will then resell the printed matter prior to use. However, since a purchaser of special printing aids from a printer would not be regarded as purchasing them for resale unless reselling them as part of the sale of the printed matter produced with those special printing aids, a printer claiming its sale of special printing aids is for resale should take a resale certificate for its sale of the printed matter as well, even if the sale of that printed matter would also qualify for exemption.</u></p> <p><u>1. Sales of printed matter to multiple purchasers. A person is not purchasing special printing aids for resale when title to the special printing aids does not pass to that person's</u></p>	<p><u>printer accepting such a resale certificate in good faith will be regarded as selling the special printing aids for resale provided the printer includes the required separately stated price for them. Otherwise, the printer will be regarded as selling the special printing aids at retail, and will owe tax on that retail sale accordingly. A printer might sell special printing aids for resale along with printed matter under circumstances where the sale of the printed matter is for resale and also qualifies for exemption, such as a sale in interstate commerce where the purchaser will then resell the printed matter prior to use. However, since a purchaser of special printing aids from a printer would not be regarded as purchasing them for resale unless reselling them as part of the sale of the printed matter produced with those special printing aids, a printer claiming its sale of special printing aids is for resale should take a resale certificate for its sale of the printed matter as well, even if the sale of that printed matter would also qualify for exemption.</u></p> <p><u>1. Sales of printed matter to multiple purchasers. Operative October 1, 2002, A person is not purchasing special printing aids for resale when title to the special printing</u></p>	<p>sales tax. This incorrect use of terminology is part of the reason that this portion of the regulation has caused confusion within the industry and among audit staff.</p>

Proposed Regulatory Changes Regarding Application of Tax to Graphic Arts and Related Enterprises
Comparison of Proposed Language for Regulation 1541
 Current as of January 16, 2002

Action Item	Current Regulatory Language	Regulatory Language Proposed by Staff	Regulatory Language Proposed by Mr. Patrick Leone (Alternative 6)	Summary Comments
		<p><u>customer prior to any use. If that person's customer does not obtain the right to exercise dominion and control over the special printing aids, the person will not be selling the special printing aids to its customer and cannot purchase the special printing aids for resale. A person does not purchase special printing aids for resale when the printed matter produced with those special printing aids is sold to several purchasers. For example, a person purchasing newspapers for individual sale cannot purchase special printing aids for resale because the individual purchasers of the newspaper are not also purchasing the special printing aids. A person purchasing posters for sale to the general public is not purchasing special printing aids for resale to the general public. A person purchasing printed cartons to pack items for individual sale is not purchasing the special printing aids used to produce the cartons for resale to the ultimate purchasers of the contents of the carton. In addition to the fact that the multiple purchasers in each of these cases could not at any time be regarded as purchasing the special printing aids, the retail purchaser of the end product is not known at the time the special printing aids are used,</u></p>	<p><u>aids does not pass to that person's customer prior to any use. If that person's customer does not obtain the right to exercise dominion and control over the special printing aids, the person will not be selling the special printing aids to its customer and cannot purchase the special printing aids for resale. A person does not purchase special printing aids for resale when the printed matter produced with those special printing aids is sold to several purchasers. For example, a person purchasing newspapers for individual sale cannot purchase special printing aids for resale because the individual purchasers of the newspaper are not also purchasing the special printing aids. A person purchasing posters for sale to the general public is not purchasing special printing aids for resale to the general public. A person purchasing printed cartons to pack items for individual sale is not purchasing the special printing aids used to produce the cartons for resale to the ultimate purchasers of the contents of the carton. In addition to the fact that the multiple purchasers in each of these cases could not at any time be regarded as purchasing the special printing aids, the retail purchaser of the end product is not known at the time the special printing aids are used,</u></p>	

Proposed Regulatory Changes Regarding Application of Tax to Graphic Arts and Related Enterprises
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		<u>could not in any event be resold to those purchasers prior to use.</u>	<u>meaning that the special printing aids could not in any event be resold to those purchasers prior to use.</u>	

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Regulation 1541. PRINTING AND RELATED ARTS.

Reference: Sections 6006-6012, Revenue and Taxation Code.

(a) DEFINITIONS.

~~—(1) SPECIAL PRINTING AID. The term “special printing aid” means a reusable manufacturing aid which is used by a printer during the printing process and is of unique utility to a particular customer. Examples of special printing aids include, but are not limited to, electrotypes, stereotypes, photoengravings, silk screens, steel dies, cutting dies, lithographic plates, artwork, film, single color, or multicolor separation negatives, and flats.~~

~~—(2) PRINTING PROCESS. The term “printing process” includes, but is not limited to, letterpress, flexography, gravure, offset lithography, reprography, screen printing, steel die engraving, thermography, laser, inkjet, and photocopying.~~

~~—(3) REPRODUCTION PROOF. A direct impression of composed type forms containing type matter only or type matter combined with clip art, or a copy of that direct impression made by any method including the diffusion transfer method, and used exclusively for reproduction.~~

~~—(4) MECHANICAL OR PASTE UP. Preparation of copy to make it camera ready with all type and design elements pasted on artboard or illustration board in exact position and containing instructions, either in the margins or on an overlay, for the platemaker. Also referred to as camera-ready art or camera-ready copy.~~

~~—(5) CLIP ART. Prepackaged art (including photographic images), not produced to the special order of the customer, commercially available on CD Rom, other electronic media or by computer program for use in digital page layout. Images that are enlarged, reduced or rotated are not considered “produced to the special order of the customer.” When distributed in digital form, clip art is often referred to as “click art”.~~

(1) CLIP ART. Clip art is prepackaged art (including photographic images) which is not produced to the special order of the customer and which is commercially available on CD ROM, other electronic media, or by computer program for use in digital page layout. Images that are enlarged, reduced, or rotated are not considered “produced to the special order of the customer.”

(2) COLOR SEPARATOR. A color separator is a person who engages in the process of color separation. The process of color separation divides a full color photographic image into four separate components, corresponding to the four primary colors used in process color printing. The color separator may accomplish this photographically or electronically, and the products of this process may be either a negative or positive film separation or a separated printing plate.

(3) COLOR SEPARATION WORKING PRODUCTS. Color separation working products consist of property such as photographic film for making transparencies, masks, internegatives, interpositives, halftone negatives, composite color separation negatives, goldenrod paper and

mylar plastic used in making flats, tape used in stripping negatives into flats, developing chemicals which become a component part of negatives and positives, proofing material and ink used in making final proofs, progressive proofs, and similar items, which are similar in function to special printing aids as defined in subdivision (a)(12).

(4) DIGITAL PRE-PRESS INSTRUCTION. Digital pre-press instruction is the creation of original information in electronic form by combining more than one computer program into specific instructions or information necessary to prepare and link files for electronic transmission for output to film, plate, or direct to press, which is then transferred on electronic media such as tape or compact disc.

(5) FINISHED ART. Finished art is the final artwork used for actual reproduction by photomechanical or other processes, or used for display. It includes electronic artwork, illustrations (e.g. drawings, diagrams, halftones, or color images), photographic images, sculptures, paintings, and handlettering.

(6) INTERMEDIATE PRODUCTION AIDS. Intermediate production aids include items such as artwork, illustrations, photographic images, photo engravings, and other similar materials which are used to produce special printing aids or other intermediate production aids.

(7) MECHANICAL OR PASTE-UP. A mechanical or paste-up (also called camera-ready art or camera-ready copy) is produced by preparing copy to make it camera-ready with all type and design elements, and then pasting the prepared copy on artboard or illustration board in exact position along with instructions, either in the margins or on an overlay, for the platemaker.

(8) PRINT BROKER. A print broker is a person who contracts to sell printed matter, but who does not actually engage in the printing process to produce the printed matter to be sold, instead purchasing the printed matter from a printer or from another print broker for resale to the print broker's customer. A person who sells printed matter for which that person did not engage in the printing process is acting as a print broker even if that person engages in the print process for other contracts.

(9) PRINTER. A printer is a person engaged in the printing process.

(10) PRINTING PROCESS. The printing process involves activities related to the production of printed matter such as letterpress, flexography, gravure, offset lithography, reprography, screen printing, steel-die engraving, thermography, laser printing, inkjet printing, and photocopying.

(11) REPRODUCTION PROOF. A reproduction proof is used exclusively for reproduction. It consists of either a direct impression of composed type forms containing type matter only or type matter combined with clip art, or a copy of that direct impression made by any method, including the diffusion transfer method.

(12) SPECIAL PRINTING AIDS. Special printing aids are reusable manufacturing aids which are used by a printer during the printing process and are of unique utility to a particular customer. Special printing aids include electrotypes, stereotypes, photoengravings, silk screens, steel dies, cutting dies, lithographic plates, film, single color or multicolor separation negatives, and flats. For purposes of this regulation, special printing aids includes items defined by subdivision (a)(6) as intermediate production aids.

(b) APPLICATION OF TAX.

~~(1) SALES BY PRINTERS. Tax applies to charges for printing of tangible personal property for consumers, regardless of whether or not the paper and other materials are furnished by the consumer. The production of printed matter for a consumer is a sale of tangible personal property whether the materials incorporated into the printed matter are furnished by the consumer or the printer. Unless that sale is exempt from tax, the measure of tax is tax applies to the total gross receipts or sales price of the sale with no deduction on account of: (a) the cost of the raw materials or other components; (b) labor or service costs of any step in the process of producing, fabricating, processing, printing, or imprinting the tangible personal property; or (c) any other expenses or services that are a part of the sale. Services that are a part of the sale of tangible personal property to consumers include, but are not limited to, charges for overtime, set-up, die cutting, embossing, folding (except as provided in subdivision (h)(g) below), and other binding operations. Printers may not deduct from the gross receipts or sales price from of their sales of printed matter charges related to their typography work or the cost of typography or typesetting to them, nor can they deduct the costs of special printing aids for which they are consumers under subdivision (c)(1)(A), whether or not a separate charge is made to the customer for the special printing aids. Receipts attributable to such costs are includable in the measure of tax.~~

Tax applies to a printer's sale of special printing aids as provided in subdivision (c).

~~(2) PURCHASES BY PRINTERS. Printers are consumers of tangible personal property which is not sold prior to use or physically incorporated into the article to be sold. Tax applies to the sale of such property to, or to the use of the property by, the a printer and also to any sale subsequent to its use by the printer. Such property includes, but is not limited to, Property ordinarily consumed by a printer includes machinery (e.g., printing presses, cameras, electronic digital pre-press equipment, and plate makers), office equipment, and printing aids. Printers, however, may purchase special printing aids for resale as explained in subdivision (c).~~

~~(c) SPECIAL PRINTING AIDS. In General. In recognition of the unique utility that special printing aids have to the sale of printed material, and the need to avoid burdening businesses with unnecessary paperwork, the following presumptions shall apply.~~

~~(1) With respect to sales of printed material ultimately subject to sales tax, or sales to the U. S. Government, it shall be presumed that the selling price of the printed material includes the selling price of the special printing aids and that title passed to the customer, irrespective of~~

~~whether or not the printer separately itemizes the special printing aids. It shall be further presumed that the printer, or other reseller, discussed in the following paragraph, made no use of the special printing aids prior to their sale. Accordingly the printer may purchase the special printing aids for resale.~~

~~“Ultimately subject to sales tax,” means either the printer's sale of the printed material and special printing aids is subject to sales tax or is an exempt sale to the U. S. Government, or if the printer's sale of the printed material is for resale, a subsequent sale of the printed material and special printing aids is subject to California sales tax or is an exempt sale to the U. S. Government.~~

~~When the printer's sale of printed material is a sale for resale, as described in the above paragraph, unless the printer timely takes a valid resale certificate in good faith that states the special printing aids are to be purchased for resale, tax is due on the selling price of the special printing aids whether or not the selling price is separately itemized. The selling price of the special printing aids is deemed to be the sales price of the special printing aids, or their components, to the printer regardless of the amount of the separately stated charge, if any, for the special printing aid. The printer need not separately charge sales tax reimbursement to their customer and if the printer has paid sales or use tax on the selling price of the special printing aids or their components to the printer, no additional tax is due.~~

~~The term “special printing aids” on a resale certificate shall be sufficient to cover all special printing aids as defined in subdivision (a)(1).~~

~~—(2) If a printer does not wish to sell special printing aids in connection with the sale of printed material ultimately subject to sales tax or sold to the U. S. Government, described in (c)(1) above, the following statement should be included on the sales invoice: “The selling price of the printed material does not include the transfer of title to the special printing aids.” The printer would then be the owner and consumer of the special printing aids. Tax would apply to both the retail sale of the printed material and the cost to the printer of the special printing aids.~~

~~—(3) With respect to all other sales of printed material, as for example, sales in interstate commerce, sales of exempt newspapers or periodicals, or sales of exempt printed sales messages, it shall also be presumed that the selling price of the printed material includes the selling price of the special printing aids and that title passed to the customer irrespective of whether or not the printer separately itemizes the special printing aids. It shall be further presumed that the printer made no use of the special printing aids prior to their sale. Sales tax is due on the selling price of the special printing aids whether or not the selling price of the special printing aids is separately stated. The selling price of the special printing aids is deemed to be the sales price of the special printing aids, or their components, to the printer regardless of the amount of the separately stated charge, if any, for the special printing aid.~~

~~The printer need not separately charge sales tax reimbursement to their customer and if the printer has paid sales or use tax on the selling price of the special printing aids or their components to the printer, no additional tax is due.~~

~~However, sales tax is not due on the selling price of the special printing aids discussed in (c)(3) if the printer timely takes a valid resale certificate in good faith that states the special printing aids are to be purchased for resale. The term "special printing aids" on a resale certificate shall be sufficient to cover all special printing aids as defined in subdivision (a)(1).~~

~~Persons issuing resale certificates for special printing aids as discussed in (c)(3) are then liable for the tax on their selling price of the special printing aids irrespective of whether or not the printer separately itemized the printing aids to the person issuing the resale certificate and notwithstanding that the printed material is exempt from tax as for example, a sale in interstate commerce, a sale of exempt newspapers or periodicals or a sale of exempt printed sales messages. In no event shall the selling price of the special printing aids be less than the selling price of the special printing aids, or their components, to the printer.~~

~~If the printer's sale includes both a sale of printed material ultimately subject to sales tax, as described in (c)(1) above, and a sale of printed material as described in (c)(3) ("split sale"), tax is due on the selling price of the special printing aids. Absent a separate itemization, as long as tax is reported on an amount equal to at least the selling price of the special printing aids or their components to the printer, no further tax will be due on the selling price of the special printing aids.~~

~~—(4) If a printer does not wish to sell special printing aids in connection with all other sales of printed material, as discussed in (c)(3) above, the following statement should be included on the sales invoice: "The selling price of the printed material does not include the transfer of title to the special printing aids." The printer would then be the owner and consumer of the special printing aids. Tax would apply to the cost to the printer of the special printing aids.~~

~~—(5) No other proof shall be required with respect to passage of title on special printing aids.~~

(c) SPECIAL PRINTING AIDS. In recognition of the unique utility that special printing aids have to the production of printed matter, the practices of the industry, and the need to avoid burdening businesses with unnecessary paperwork, the presumptions and rules set forth in this subdivision apply to a printer's purchase and sale of special printing aids used to produce printed matter sold by the printer.

(1) PRINTER'S PURCHASE OF SPECIAL PRINTING AIDS.

(A) When a printer who uses special printing aids to produce printed matter does not wish to sell those special printing aids in connection with the printer's sale of the printed matter so produced, the printer shall include the following or substantially similar statement in the contract or the sales invoice: "Special printing aids are not being sold to the customer as part of the sale

of the printed matter, and the selling price of the printed matter does not include the transfer of title to the special printing aids.” When this statement, or a substantially similar statement, is included in the contract or sales invoice, the printer retains title to the special printing aids and is the consumer thereof, without regard to whether the printer separately itemizes a charge for the special printing aids. Accordingly, the printer may not issue a resale certificate to purchase such special printing aids for resale, and tax applies to the cost to the printer of those special printing aids.

(B) Unless the printer includes a statement in the contract or sales invoice retaining title to the special printing aids, as described in subdivision (c)(1)(A), it shall be irrebuttably presumed that the printer resold to the customer the special printing aids purchased or produced by the printer for use on the customer’s job, prior to any use, along with the printed matter produced with the special printing aids, without regard to whether the printer separately itemizes a charge for the special printing aids. Accordingly, unless the printer includes a statement in the contract or sales invoice retaining title, the printer may issue a resale certificate when purchasing such special printing aids or their components. If the vendor of the special printing aids to the printer does not take a valid and timely resale certificate from the printer stating that the special printing aids are for resale, the vendor has the burden of showing that the printer actually resold the special printing aids prior to use as provided in this subdivision.

(2) PRINTER’S SALE OF SPECIAL PRINTING AIDS. When the printer is regarded as purchasing the special printing aids for resale under subdivision (c)(1)(B), the following rules apply to determine the application of tax to the printer’s sale of those special printing aids along with the printed matter produced with the special printing aids.

(A) Retail Sales of Special Printing Aids.

1. Sales to the United States Government. When a printer makes a retail sale of special printing aids along with the printed matter produced with those special printing aids to the United States Government, the sale of the printed matter and the special printing aids to the United States Government is exempt from tax as provided in Regulation 1614.

2. With nontaxable sale of printed matter. When a printer makes a retail sale of special printing aids to anyone other than the United States Government along with a nontaxable sale of printed matter (such as an exempt sale in interstate commerce, an exempt sale of qualifying newspapers, periodicals, or printed sales messages, or a nontaxable sale for resale), the printer’s sale of the special printing aids is subject to sales tax. The printer’s taxable gross receipts or sales price from the sale of the special printing aids is deemed to be the sale price of the special printing aids, or their components, to the printer without regard to whether the printer separately states a charge for the special printing aids or, if the printer does so, without regard to the amount of that separately stated charge, and tax is due measured by that sale price. If the printer has paid California sales tax reimbursement or use tax on the sale price of the special printing aids or their components to the printer, no additional tax is due.

3. With taxable sale of printed matter. When a printer makes a retail sale of special printing aids along with the taxable retail sale of printed matter, tax applies to the entire charge for the printed matter and special printing aids, without regard to whether the charge for the special printing aids is separately stated. If the printer does not make a separate charge for the special printing aids, the charge for the printed matter is deemed to include the taxable charge for the special printing aids, and no further tax is due on account of the sale of those special printing aids.

(B) Nontaxable Sales of Special Printing Aids for Resale. A person purchasing printed matter for resale may also purchase the special printing aids used to produce the printed matter for resale if that person will, in fact, resell the special printing aids prior to any use. A printer will not be regarded as selling special printing aids for resale unless: 1) the printer separately states the sale price of the special printing aids in an amount not less than the sale price of the special printing aids, or their components, to the printer; and 2) the printer accepts a timely and valid resale certificate in good faith from the printer's customer stating that the special printing aids are purchased for resale. The term "special printing aids" on a resale certificate shall be sufficient to cover all special printing aids as defined in subdivision (a)(12), and a printer accepting such a resale certificate in good faith will be regarded as selling the special printing aids for resale provided the printer includes the required separately stated price for them. Otherwise, the printer will be regarded as selling the special printing aids at retail, and will owe tax on that retail sale accordingly. A printer might sell special printing aids for resale along with printed matter under circumstances where the sale of the printed matter is for resale and also qualifies for exemption, such as a sale in interstate commerce where the purchaser will then resell the printed matter prior to use. However, since a purchaser of special printing aids from a printer would not be regarded as purchasing them for resale unless reselling them as part of the sale of the printed matter produced with those special printing aids, a printer claiming its sale of special printing aids is for resale should take a resale certificate for its sale of the printed matter as well, even if the sale of that printed matter would also qualify for exemption.

1. Sales of printed matter to multiple purchasers. A person is not purchasing special printing aids for resale when title to the special printing aids does not pass to that person's customer prior to any use. If that person's customer does not obtain the right to exercise dominion and control over the special printing aids, the person will not be selling the special printing aids to its customer and cannot purchase the special printing aids for resale. A person does not purchase special printing aids for resale when the printed matter produced with those special printing aids is sold to several purchasers. For example, a person purchasing newspapers for individual sale cannot purchase special printing aids for resale because the individual purchasers of the newspaper are not also purchasing the special printing aids. A person purchasing posters for sale to the general public is not purchasing special printing aids for resale to the general public. A person purchasing printed cartons to pack items for individual sale is not purchasing the special printing aids used to produce the cartons for resale to the ultimate purchasers of the contents of the carton. In addition to the fact that the multiple purchasers in each of these cases could not at any time be regarded as purchasing the special printing aids, the retail purchaser of the end product is not known at the time the special printing aids are used,

meaning that the special printing aids could not in any event be resold to those purchasers prior to use.

2. Existing obligation to resell special printing aids. A person cannot purchase special printing aids for resale when that person does not have an existing obligation to resell those particular special printing aids since, if the purchaser does not have such an existing obligation to resell the special printing aids, the printer will use them on the purchaser's behalf before they could be resold by the purchaser. An existing obligation may be represented by a purchase order, invoice, or other existing agreement, whether oral or in writing. If the existing obligation is an oral agreement, the person purchasing the special printing aids for resale must have some means to establish that the agreement was in existence no later than the time the special printing aids were used in the printing process.

(C) Split Sales. A printer may use special printing aids to produce printed matter where a portion of the sale is taxable and a portion of the sale is not taxable, such as the sale of printed sales messages some of which are delivered as required for exemption by Regulation 1541.5 and some of which are delivered directly to the purchaser. If a printer makes a sale of printed matter where a portion of the sale is taxable and a portion is not taxable along with a retail sale of the special printing aids used to produce that printed matter, tax is due on the full sale price of the special printing aids. If the printer separately states a charge for the special printing aids in an amount not less than the sale price of the special printing aids or their components to the printer, tax applies to that separate charge. In the absence of such a separate charge, the taxable portion of the sale of printed matter will be regarded as including the sale of the special printing aids provided that the measure of tax on that sale is at least equal to the sale price of the special printing aids or their components to the printer. If so, no further tax is due for the printer's sale of the special printing aids. If the measure of tax on the sale of the printed matter is less than the sale price of the special printing aids or their components to the printer, then the printer owes tax on the difference.

(3) PURCHASES AND SALES OF SPECIAL PRINTING AIDS BY PRINT BROKERS.

(A) Print Broker's Purchase of Special Printing Aids for Resale. A person who purchases special printing aids for resale with printed matter but who will not itself use those special printing aids in the printing process is a print broker for that purchase and resale. A print broker who will acquire title to special printing aids from a printer or other print broker will be irrebuttably presumed to have resold the special printing aids to the customer, prior to any use, along with the printed matter produced with the special printing aids provided the print broker has, at the time of acquisition of the special printing aids, an existing obligation with a customer for the sale of printed matter and the print broker does not include a statement in the contract or sales invoice retaining title to the special printing aids, as described in subdivision (c)(1)(A). Accordingly, unless the print broker includes a statement in the contract or sales invoice retaining title, the print broker may purchase such special printing aids for resale pursuant to its existing obligation and issue a resale certificate for both the special printing aids and the printed matter. However, without regard to the taking of a resale certificate, a printer or print broker is

regarded as making a retail sale of the special printing aids, and not a sale for resale, unless the printer or print broker separately states the charge for those special printing aids, which charge cannot be less than the sale price of such printing aids, or their components, to the printer.

(B) Print Broker Issuing Resale Certificate. A print broker who issues a resale certificate for the purchase of special printing aids is liable for tax on the print broker's sale price of the special printing aids, even if the print broker's sale of the printed material produced with the special printing aids is not subject to tax (such as an exempt sale in interstate commerce, an exempt sale of qualifying newspapers, periodicals, or printed sales messages, or a nontaxable sale for resale), unless the print broker sells the special printing aids to the United States Government or to another print broker who issues a timely and valid resale certificate in good faith as provided in this subdivision (c).

(C) Print Broker's Retail Sales of Special Printing Aids.

1. Sales to the United States Government. When a print broker who purchases special printing aids under a resale certificate sells those special printing aids along with the printed matter produced with those special printing aids to the United States Government, the sale of the special printing aids to the United States Government is exempt from tax as provided in Regulation 1614.

2. With nontaxable sale of printed matter. When a print broker who purchases special printing aids under a resale certificate makes a retail sale of special printing aids to anyone other than the United States Government along with a sale of printed matter that is not taxable (such as an exempt sale in interstate commerce, an exempt sale of qualifying newspapers, periodicals, or printed sales messages, or a nontaxable sale for resale), that sale of the special printing aids is subject to tax. If the print broker separately states a charge for the special printing aids that is not less the printer's separately stated sale price for the special printing aids to the print broker, then tax applies to that separately stated sale price. Otherwise, tax applies to the the print broker's sale of the special printing aids measured by the printer's separately stated sale price to the print broker.

3. With taxable sale of printed matter. When a print broker who purchases special printing aids under a resale certificate makes a retail sale of those special printing aids along with the taxable retail sale of printed matter, tax applies to the entire charge for the printed matter and special printing aids, without regard to whether the charge for the special printing aids is separately stated. If the print broker does not make a separate charge for the special printing aids, the charge for the printed matter is deemed to include the taxable charge for the special printing aids, and no further tax is due on account of those special printing aids.

4. Split Sales. A print broker may sell special printing aids to produce printed matter the sale of which is partially exempt and partially subject to tax, such as the sale of printed sales messages some of which are delivered as required for exemption by Regulation 1541.5 and some of which are delivered directly to the purchaser. If a print broker makes a sale of printed matter

where a portion of the sale is taxable and a portion is not taxable along with a retail sale of the special printing aids used to produce that printed matter, tax is due on the full sale price of the special printing aids. If the print broker separately states a charge for the special printing aids in an amount not less than the printer's separately stated sale price of the special printing aids to the print broker, tax applies to that separate charge. In the absence of such a separate charge, the taxable portion of the sale of printed matter will be regarded as including the sale of the special printing aids provided that the measure of tax on that sale is at least equal to the printer's separately stated sale price of the special printing aids to the print broker; if so, no further tax is due for the print broker's sale of the special printing aids, but if the measure of tax on the sale of the printed matter is less than the printer's separately stated sale price of the special printing aids to the print broker, then the print broker owes tax on the difference.

(d) CONCEPTUAL SERVICES.

(1) When the printer makes a lump sum charge for a taxable sale of printed matter, the full lump sum charge is subject to tax with no deduction on account of any conceptual or other services performed to produce that printed matter. When the printer itemizes its charges for a taxable sale of printed matter, tax applies to the printer's entire charge except as provided below.

(2) As part of its contract to produce and sell printed matter, a printer may also agree to acquire finished art for use in producing the printed matter, and the acquisition of that finished art may involve the providing of services to convey ideas, concepts, looks, or messages to a printer's customer which result in a transfer, enhancement, or revision of either electronic artwork, hard copies of electronic artwork, or copies of manually prepared artwork. If the printer states a separate charge for such services which are itemized as "design charges," "preliminary art," "concept development," or any other designation that clearly indicates that the charges are for such services and not for finished art, they are nontaxable unless the contract of sale provides that the printer will pass to its customer title or the right to permanent possession of the artwork in tangible form, such as on electronic media or hard copy, or permanent possession of the artwork in tangible form is, in fact, transferred to the client. The remainder of the printer's charge is subject to tax.

(3) If a printer separately itemizes charges for finished art that also include charges for conceptual services described in subdivision (d)(2), it will be rebuttably presumed that 75 percent of the combined charge for the finished art and conceptual services is for the nontaxable services. If, however, the printer acquires the finished art and conceptual services from a commercial artist (rather than producing the finished art itself) and the commercial artist itemizes a separate charge for conceptual services that is less than 75 percent of the commercial artist's combined charge for conceptual services and finished art, that lesser percentage shall be applied to the printer's combined charge for final art and conceptual services to determine the total nontaxable charges for conceptual services. Tax applies to the remaining portion of the combined charge for final art and conceptual services unless: 1) the printer passes title to the final art to its customer; and 2) that transfer qualifies a technology transfer agreement under subdivision (b)(2)(D)2 of Regulation 1540, in which case tax applies to the charge for finished

art in accordance with that provision. A separately itemized charge for special printing aids is not a separately itemized charge for finished art and conceptual services, and no portion of that charge is excluded from tax as a charge for nontaxable conceptual services.

~~(d)~~(e) COLOR SEPARATORS. The application of tax to printers as explained in this regulation subdivisions (b) and (c) also applies to color separators. Color separators are consumers and not retailers of tangible personal property which is not sold prior to use or physically incorporated into the article to be sold. Tax applies to the sale of such property to, or to the use of such property by, the color separator. Examples of such property include, but are not limited to, filters and screens, trial proofing materials, disposable lithographic plates, and developing chemicals which do not become incorporated into the article sold. Color separator working products are special printing aids for purposes of this regulation, and the provisions of subdivision (c) apply to their purchase and sale. Color separators, and persons such as printers when acting as color separators, or printers may purchase property such as photographic film for making transparencies, masks, internegatives, interpositives, halftone negatives, composites color separation negatives, goldenrod paper and mylar plastic used in making flats, scotch tape used in stripping negatives into flats, developing chemicals which become a component part of negatives and positives, proofing material and ink used in making final proofs, progressive proofs, and similar items, which are similar in function to special printing aids as defined in subdivision (a)(8) (a)(1), all commonly referred to as "color separator working products" for resale when title to such property passes to the customer prior to use by the color separator or the printer as described in subdivision (c). The term "color separator working products" or "special printing aids" on a resale certificate shall be sufficient to cover all such products.

Charges for alterations of film work for \$100 or less shall be considered charges for restoring property to its original condition and not subject to tax. Charges greater than \$100 shall be considered charges for fabrication labor and subject to tax.

~~(e)~~(f) COMPOSED TYPE.

(1) IN GENERAL. Tax does not apply to the fabrication or transfer by a typographer or typesetter of composed type, or reproduction proofs of such composed type to printers to use in the preparation of printed matter. The composition of type is the performance of a service, and tax does not apply to charges for such service, unless that service is a part of the sale of printed matter. Tax applies to the gross receipts from the sale of printed matter without any deduction for the charge for typography. Tax applies See subdivision (e)(3) below for the application of tax to charges for transfers of composed type combined with artwork as provided in subdivision (f)(3).

Typographers and typesetters are the consumers and not retailers of materials, such as typesetting machinery, metal forms, galleys, proofing paper, and cleaners which are used in the performance of their service and are consumers of materials transferred to their customers incidental to the performance of nontaxable typography or typesetting services, such as clip art that is combined with text on the same page.

Composed type includes type together with lined borders and plain, straight, fancy, or curved lines. Composed type also includes charts, tables, graphs, and similar methods of providing information.

(2) PHOTOCOMPOSITION (INCLUDING PHOTOTYPESETTING AND COMPUTER TYPESETTING). Tax does not apply to the composing of type regardless of whether the type is composed by means of such simplified methods as standard typewriter, desktop publishing, Varityper or Justowriter; by means of photolettering or headlining machines; or by means of a photocomposition (including computer photocomposition) method. Tax does not apply to the transfer, whether temporary or permanent, of the direct product of the type composition service or copy thereof (e.g., typeset matter direct from the typesetting machine ready to be cut and pasted up for reproduction or computer generated type), if that product contains text only or text combined with clip art, whether that product is a paper or film (negative or positive) product, provided the product or copy is to be used exclusively for reproduction.

The transfer of camera-ready copy containing text only or text and clip art in the form of a paste-up, mechanical, or assembly, or a camera-ready reproduction of such, is the transfer of composed type and the charge made by the typographer or typesetter to his or her customer is not subject to tax. Tax does not apply to the transfer of a direct photoreproduction of type composed by means of a photolettering or headlining machine or other similar device.

Camera-ready copy which is produced through the use of desktop publishing software and a personal computer is nontaxable composed type provided it does not contain artwork other than clip art.

Transfers of plates and mats for use in the printing process which are produced using composed type are subject to tax, and tax applies to the entire charge made to the customer including any portion of the charge attributable to the type composition service, whether that charge is separately stated or not. Transfers of engraved printing plates and duplicate plates such as electrotypes, plastic plates, rubber plates, and other plates used in letterpress printing are subject to tax. Similarly, transfers of exposed presensitized, wipe-on, deep-etch, bi-metal and other plates used in offset lithography or of exposed plates produced by a photo-direct method, do not qualify as transfers of reproduction proofs of composed type and are subject to tax. A transfer of gelatin coated film to be transferred to fine mesh silk in the silk-screening process is subject to tax.

(3) ARTWORK. Artwork, other than clip art combined with composed type on the same page, is not composed type. The term "artwork" includes, ~~but is not limited to,~~ illustrations (e.g., drawings, diagrams, halftones, or color images), photographic images, drawings, paintings, handlettering, and computer generated artwork. If the basis for billing is on a per page basis, the charge for any page with artwork is subject to sales tax and the charge for any page with only text, or text and clip art, is not subject to tax. If the basis for billing is lump sum, the ratio of pages containing artwork to the total number of pages, applied to the lump sum charge,

represents the retail ~~selling-sale~~ price of the artwork and is subject to tax, but in no event shall the retail ~~selling-sale~~ price of the artwork be less than the ~~selling-sale~~ price of the artwork, or its components, to the typographer.

However, if ~~the ratio computed above is 10% or less ten percent or fewer of the pages contain~~ artwork, the true object of the sale shall be deemed to be a sale of typography services with an incidental transfer of artwork, and the typographer is the consumer of ~~the that~~ artwork. Tax applies to the ~~selling-sale~~ price of the artwork, or its components, to the typographer. Tax does not apply to the sale of the typography service as explained in ~~(e)(1)~~ subdivision (f)(1).

(4) REPRODUCTION RIGHTS. Notwithstanding subdivision (f)(3), if the transfer of artwork qualifies as a technology transfer agreement under subdivision (b)(2)(D)2. of Regulation 1540, tax applies to the transfer of the artwork in accordance with that provision.

(f)(g) TRANSFERS OF INFORMATION ON COMPUTER DISK OR OTHER ELECTRONIC MEDIA-DIGITAL PRE-PRESS INSTRUCTION.

The transfer by the seller of the original information created by combining more than one computer program into specific instructions or information necessary to prepare and link files for electronic transmission for output to film, plate, or direct to press, is not subject to tax when transferred by computer disk or other electronic storage media and the original information is a custom computer program. Such a process, currently termed "electronic or digital pre-press instruction," creates a new program which shall be considered Digital pre-press instruction is a custom computer program as defined under section 6010.9 of the Revenue and Taxation Code, the sale of which and is not subject to tax, provided if the electronic or digital pre-press instruction is prepared to the special order of the purchasercustomer. The electronic or dDigital pre-press instruction shall not, however, be regarded as a custom computer program if it is a "canned" or prewritten computer program which is held or existing for general or repeated sale or lease, even if the electronic or digital pre-press instruction was initially developed on a custom basis or for in-house use. The sale of such canned or prewritten digital pre-press instruction in tangible form is a sale of tangible personal property, the retail sale of which is subject to tax.

(g)(h) MAILING. Tax does not apply to charges for postage or for addressing for the purpose of mailing (by hand or by mechanical means), folding for the purpose of mailing, enclosing, sealing, preparing for mailing, or mailing letters or other printed matters, provided such charges are stated separately on invoices and in the accounting records. Tax applies, however, to charges for envelopes.

(h)(i) SIGNS, SHOW CARDS, AND POSTERS. Tax applies to retail sales of signs, show cards, and posters, and to charges for painting signs, show cards, and posters, whether the materials are furnished by the painter or by the customer.

Tax does not apply to charges for painting or lettering on real property. The painter or letterer is the consumer of the materials used in such work, and tax applies with respect to the sale of such property to or the use of such property by, the painter or letterer ~~him~~.

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Regulation 1543. PUBLISHERS.

Reference: Sections 6006, ~~6007~~, ~~6010~~, ~~6010.3~~, ~~6011~~, ~~6012~~, ~~6015~~, 6094, 6244, 6362, 6379.5 and 6396, Revenue and Taxation Code.

(a) DEFINITIONS.

~~—(1) AUTHOR. Author means and includes any person who creates an original manuscript for the purpose of publication. For purposes of this regulation, the following persons are also authors:~~

~~—(A) Developmental Editors. A developmental editor means and includes any person who consults with an author (as defined above) to develop the concepts in a manuscript or reviews the copy edited manuscript and recommends visual concepts.~~

~~—(B) Copy Editors. A copy editor means and includes any person who reviews a manuscript for grammatical consistency and clarity.~~

~~—(C) Manuscript Reviewers. A manuscript reviewer means and includes any person who reviews a manuscript for technical accuracy and acceptability to the proposed audience. For example, a reviewer may review the manuscript of a book on gardening for technical accuracy and suitability of the gardening advice for a particular climate.~~

~~—(D) Photo researchers. A photo researcher means and includes any person who assists other authors or publishers in obtaining permission and rights from third parties to use photographic images to illustrate a manuscript.~~

~~—(E) Translators. A translator means and includes any person who produces a manuscript that is a translation of material from a different language.~~

~~—(2) DESIGNER. Designer means and includes any person who plans and prepares a general layout of typographical and illustrative elements for printed literature.~~

~~—(3) ART DIRECTOR. Art Director means and includes any person who prepares general specifications (in the form of verbal instructions or rough sketches) for an illustrator or photographer.~~

~~—(4) PRODUCTION FUNCTION. A production function is a segment of the process of producing camera ready art or camera ready copy, and includes but is not limited to the following:~~

~~—(A) Manuscript Mark-Up: The application of type specifications to a manuscript for typesetting, when done manually.~~

~~—(B) Formatting: Manuscript mark-up, when done electronically.~~

~~—(C) **Typesetting, Typography or Composition:** Composition of type by any method, within the meaning of Revenue and Taxation Code section 6010.3.~~

~~—(D) **Proofreading:** A reading of typeset copy for correctness in comparison with the original manuscript.~~

~~—(E) **Alterations:** Changes made to typeset copy or camera-ready copy.~~

~~—(F) **Dummy:** A mock-up or layout of a page showing position and overall form, used for approval. A dummy can be assembled manually or generated by a computer program. A dummy is never incorporated physically into a mechanical or paste-up.~~

~~—(G) **Mechanical or Paste-up.** Reproduction (“repro”) copy, both text and illustrative material, that is ready to be photographed and made into lithographer's film. Also referred to as camera-ready art or camera-ready copy.~~

~~—(H) **Production Coordination or Production Direction:** Coordination and scheduling of the various components of a project.~~

~~—(I) **Production Editing:** Maintaining editorial integrity of the author's work during the production process.~~

~~—(5) **PUBLISHER.** Publisher means and includes any person who owns the rights to reproduce, market and distribute printed literature.~~

~~—(6) **PRELIMINARY ART.** Preliminary art means roughs, visualizations, layouts and comprehensives, title to which does not pass to the client, but which are prepared solely for the purpose of demonstrating an idea or message for acceptance by the client before a contract is entered into or before approval is given for preparation of finished art to be furnished by the seller to his or her client.~~

~~—(7) **FINISHED ART.** Finished art means the final art used for actual reproduction by photo-mechanical or other processes.~~

~~—(8) **PHOTOSTAT.** Photostat means a copy produced by photographic means, often used in layout, dummy work, or “for position only” on camera-ready art.~~

~~—(9) **SYNDICATORS.** The term syndicator means and includes any person who receives original manuscripts or reproduction proofs thereof, including columns, cartoons, and comic strip drawings, from authors and distributes those manuscripts to publishers for publication.~~

(1) **ART DIRECTOR.** An art director prepares general specifications (in the form of verbal instructions or rough sketches) for an illustrator or photographer.

(2) AUTHOR. An author creates an original manuscript, whether written by hand, on a typewriter or computer, or otherwise, for the purpose of publication. For purposes of this regulation, the following persons are also authors:

(A) Copy editor, who reviews a manuscript for grammatical consistency and clarity.

(B) Developmental editor, who consults with the author who created an original manuscript for purposes of publication to develop the concepts in the manuscript, or who reviews the copy edited manuscript and recommends visual concepts.

(C) Manuscript reviewer, who reviews a manuscript for technical accuracy and acceptability to the proposed audience. For example, a reviewer may review the manuscript of a book on gardening for technical accuracy and suitability of the gardening advice for a particular climate.

(D) Photo researcher, who assists other authors or publishers in obtaining permission and rights from third parties to use photographic images for purposes of reproduction in the publication of a manuscript.

(E) Translator, who produces a manuscript that is a translation of material from a different language.

(3) DESIGNER. A designer plans and prepares a general layout of typographical and illustrative elements for printed literature.

(4) FINISHED ART. Finished art is the final artwork used for actual reproduction by photomechanical or other processes, or used for display. It includes electronic art, illustrations (e.g. drawings, diagrams, halftones, or color images), photographic images, sculptures, paintings, and handlettering.

(5) ILLUSTRATOR. An illustrator creates an illustration, which is an original artwork (including cartoons and comic strips) licensed for the purpose of publication.

(6) PHOTOGRAPHER. A photographer creates an original photographic image through the use of a camera or similar device, which photographic image is licensed for the purpose of publication.

(7) PHOTOSTAT. A photostat (also called a “stat”) is a copy produced by photographic means, often used in layout, dummy work, or “for position only” on camera-ready art.

(8) PRELIMINARY ART. Preliminary art is tangible personal property which is prepared solely for the purpose of demonstrating an idea or message for acceptance by the client before a contract is entered into or before approval is given for preparation of finished art to be furnished or licensed by the seller to his or her client, provided neither title to nor permanent possession of

such tangible personal property passes to the client. Preliminary art may include roughs, visualizations, layouts, comprehensives, and instant photos.

(9) PRODUCTION FUNCTION. A production function is a segment of the process of producing camera-ready art or camera-ready copy, and includes the following:

(A) Alterations, which are changes made to typeset copy or camera-ready copy.

(B) Dummy, which is a mock-up or layout of a page showing position and overall form, used for approval. A dummy can be assembled manually or generated by a computer program. A dummy is never physically incorporated into a mechanical or paste-up.

(C) Formatting, which is a manuscript mark-up, when done electronically.

(D) Manuscript mark-up, which is the application of type specifications to a manuscript for typesetting, when done manually.

(E) Mechanical or paste-up (also called camera-ready art or camera-ready copy), which is produced by preparing copy to make it camera-ready with all type and design elements, and then pasting the prepared copy on artboard or illustration board in exact position along with instructions, either in the margins or on an overlay, for the platemaker.

(F) Production Coordination or Production Direction, which is the coordination and scheduling of the various components of a project.

(G) Production Editing, which is editing that maintains editorial integrity of the author's work during the production process.

(H) Proofreading, which is a reading of typeset copy for correctness in comparison with the original manuscript.

(I) Typesetting, typography, or composition, which is the fabrication or production of composed type, or reproduction proofs thereof, for use in the preparation of printed matter. Typesetting, typography, or composition does not include the fabrication or production of a paste-up, mechanical, or assembly of which a reproduction proof is a component part.

(10) PUBLISHER. A publisher owns, outright or by license, the rights to reproduce, market, and distribute printed literature.

(11) SYNDICATOR. A syndicator receives from authors original manuscripts, or reproduction proofs thereof, including columns, cartoons, and comic strip drawings, and distributes those manuscripts to publishers for publication.

(b) APPLICATION OF TAX.

(1) AUTHORS.

(A) The transfer by an author to a publisher or syndicator, for the purpose of publication, of an original manuscript or copy thereof, including the transfer of an original column, cartoon, or comic strip drawing, is a service, the charge for which is not subject to sales tax ~~not subject to taxation. Tax does not apply even if the manuscript is transferred in machine-readable form. The transfer of any paper, tape, diskette or other tangible personal property transferred as a means of expressing an idea is not taxable.~~ If the author transfers the original manuscript or copy thereof in tangible form, such as on paper or in machine-readable form such as on tape or compact disc, that transfer is incidental to the author's providing of the service, and the author is the consumer of any such property. However, ~~tax applies to the sale of the transfer of mere copies of an author's work is a sale of tangible personal property, and tax applies accordingly.~~

(B) Tax applies to charges for transfers of photographic images and illustrations, whether or not the photographic images or illustrations are copyrighted. Transfers of photographic images or illustrations illustrating text written by the photographer or illustrator are not taxable when they are merely incidental to the editorial matter.

(2) SYNDICATORS. The transfer by a syndicator to a publisher of impressed mats or proofs of syndicated columns, cartoons, or comic strip drawings for the purpose of publication is not subject to tax.

(3) DESIGNERS AND ART DIRECTORS. Fees paid to a designer or art director for his or her ability to design, conceive, or dictate ideas, concepts, or specifications are not subject to tax if the designer or art director does not transfer to the client or to any other person on behalf of the client title or possession of any tangible personal property used to convey the ideas. The designer or art director is the consumer of any paper, tape, film, diskette, or other tangible personal property used. Tax applies to the sale of such tangible personal property to, or use of such tangible personal property by, the designer or art director.

(4) PRODUCTION FUNCTIONS.

(A) Tax applies to the gross receipts from the retail sale of camera-ready art or camera-ready copy. The measure of tax includes charges for the performance of all production functions, whether the charges are separately stated or not.

(B) A contract under which a person performs only the following functions (or any combination of the following functions) ~~only~~ is not subject to tax: ~~Manuscript mark-up, formatting, typesetting, proofreading, production coordination, and production editing.~~ Charges for any of such functions are taxable when they are provided as part of the taxable sale of camera-ready copy or camera-ready art unless, are separable in the sense that there is no contract for the camera-ready copy or camera-ready art until after such functions are completed, in which case the charges for such functions are nontaxable.

(5) **CONTRACT TO PERFORM SERVICES AND TO FURNISH TANGIBLE PERSONAL PROPERTY.** One person may, under a single agreement, contract both to perform author, design, or art direction services, and to produce camera-ready copy or art. If, under the terms of the agreement, the client retains the right to approve the manuscript, layout, or general specifications before authorizing preparation of camera-ready copy or art, and if the author, designer, or art director does not transfer to the client title to the layouts or possession of the layouts other than for the purpose of review and approval only, then separately stated charges for performance of the services are not taxable. In the absence of specific contractual language, proof of client approval shall be evidenced by contemporaneous notation of receipt of approval in the records of the author, designer, or art director. No other proof shall be required.

(6) ~~ILLUSTRATIONS~~ **PRELIMINARY ART.** Tax does not apply to separately stated charges for preliminary art, except where the preliminary art becomes physically incorporated into the finished art, as, for example, when the finished art is made by inking directly over a pencil sketch or drawing, or the approved layout is used as camera copy for reproduction. The charge for preliminary art is separately stated if it is must be billed separately to the client, either on a separate billing or separately charged for itemized on the billing for the finished art. ~~It must be provided it is~~ clearly identified on the billing as roughs, visualizations, layouts, comprehensives, or other preliminary art. Proof of ordering or producing the preliminary art, prior to the date of the contract or approval for finished art, shall be evidenced by purchase orders of the buyer, or by work orders or other records of the seller. No other proof shall be required. Tax applies to the total charges made for finished art. If there is no separately stated charge for preliminary art, then there is no deduction for such services from the taxable measure for the sale of the finished art except as provided in subdivision (b)(2)(C) of Regulation 1540.

(7) **SALES BY PUBLISHERS.** Sales of printed literature are subject to tax unless the sale is for resale or is specifically exempted by law, e.g., qualifying sales of printed sales messages and sales in interstate and foreign commerce.

(8) **TRANSPORTATION CHARGES AND SERVICES RELATED TO TRANSPORTATION.** ~~In general, tax applies to charges for the transportation of printed matter in connection with a taxable retail sale except as provided in tangible personal property except under certain conditions. For rules relating to transportation charges, see Regulation 1628, Transportation Charges.~~

Separately stated charges for services such as addressing (by hand or by mechanical means), folding, enclosing, or sealing directly related directly to the transportation of printed material matter to the customer are not subject to the tax, e.g., ~~addressing (by hand or by mechanical means), folding, enclosing, or sealing.~~ Tax applies, however, to charges for envelopes except as otherwise provided in Regulation 1541.5.

(9) **PURCHASES OF PROPERTY FOR RESALE.** Tax applies to the purchase of tangible personal property that is consumed in any production function and does not become a part of the finished product. However, a person may purchase such property for resale if that person's contract of sale with its client explicitly passes title to the property passes to that person's client

prior to its use. Tangible personal property so purchased must be separately listed and priced on the person's sales invoice to the client ~~and sales tax charged when appropriate and sales tax applies to that charge.~~ ~~Art work is considered to be used if it is photocopied. If artwork is purchased together with a photostat of the artwork and the purchaser uses only the photostat but not the artwork, the artwork may be purchased for resale. Tax applies to the charge made for the photostat.~~

(10) REPRODUCTION RIGHTS. Notwithstanding anything to the contrary in this regulation, if the transfer of a photographic image or artwork is made pursuant to a technology transfer agreement under subdivision (b)(2)(D)2. of Regulation 1540, tax applies to the transfer of the artwork in accordance with that provision.

(c) EXAMPLES OF THE APPLICATION OF TAX UNDER SPECIFIC CIRCUMSTANCES.

(1) A firm provides various services to a publisher. In performing a contract with the publisher, the firm buys a color separation from a third party. The firm does not make a copy of the color separation or use it in any way, but resells it to the publisher. The firm may give a resale certificate to the third party but tax applies to the sale to the publisher.

(2) The firm in Example (1) uses the color separation before reselling it to the publisher. Both the firm and the publisher are consumers, and both sales are subject to tax.

(3) The firm in Example (1) buys both the color separation and a photostatic copy ("stat") of it from the third party who separately states the price of each item on his sales invoice. The firm retains the ~~stat photostatic copy~~ but resells the color separation to the publisher without using it in any way. Since the third party used the color separation to make a copy of it, the sale of the component parts to the third party, or the third party's use of those component parts, is subject to tax. The firm may give a resale certificate to the third party for the color separation, but tax applies to the third party's sale of the ~~stat photostatic copy~~. Tax also applies to the firm's sale of the color separation to the publisher.

(4) A firm contracts with a publisher to perform a contract in three stages, as follows:

(A) The firm creates an original manuscript of a book. The publisher reviews the first draft, comments on it, and approves it. The firm then does developmental editing, in which the writer and editors develop the manuscript for sound editorial structure and organization. The publisher reviews the resulting second draft, comments on it, and approves it. The firm then does copy editing, in which editors review the manuscript for grammatical consistency and clarity. After this, the firm passes title to the manuscript to the publisher for the purpose of publication. Under the contract, the firm can proceed with further work only with the publisher's approval.

Tax does not apply to the sale of the finished manuscript or to any of the steps of writing and editing it.

(B) In the second stage, the publisher returns the accepted manuscript to the firm for typesetting into galleys, which the publisher reviews and approves. The firm then arranges the galleys into page form, which the publisher reviews and approves. The firm then produces camera-ready art, which the publisher reviews for approval or alterations. The publisher then accepts and takes title to the camera-ready art.

Tax applies to the firm's gross receipts from the sale of the camera-ready art, including formatting, typesetting, proofreading, and production coordination, whether separately stated or not. To preserve the ~~exempt nontaxable~~ status of the receipts described in Example (4)(A), ~~above, the receipts~~ charges for work done in Example (4)(A) should must be separately stated from the receipts ~~charges for the sale of the tangible personal property in this Example (4)(B).~~

(C) In the third stage, the publisher returns the camera-ready art to the firm for printing. The firm subcontracts the printing to a printer. The firm manages the quality of the printing. A representative of the publisher visits the printer to approve the work. At the firm's instruction, the printer ships the completed books to the publisher's warehouse.

~~The~~ Since the firm will be reselling the books to the publisher without using them, the firm may issue a resale certificate to the printer. Since the publisher intends to resell the books, the publisher may furnish issue a resale certificate to the firm, who may in turn furnish a resale certificate to the printer (provided the firm does not use the completed books in any way). Tax applies to sales of the books by the publisher to consumers unless the sales are specifically exempt by statute (e.g., sales in interstate commerce).

(5) A publisher owns an existing manuscript. The publisher contracts with an editorial design firm for developmental editing, copy editing, and design specifications. The firm reviews the manuscript and makes recommendations to the publisher for developing it into publishable form, including recommended layout and a general approach to design (e.g., trim size). After the publisher accepts these recommendations, a designer (at the firm or a subcontractor) prepares sample sketches and dummies to express the idea to the publisher. After the publisher approves the sketches and dummies, the designer creates type specifications. A developmental editor and a copy editor (at the firm or a subcontractor) perform development and copy editing services. The edited manuscript, dummies, and type specifications are transferred to the publisher.

Tax does not apply to the editing services because they are author's services. Tax does not apply to charges for the dummies and type specifications ~~the charges for the dummies and type specifications~~ those charges are separately stated and if possession and title is retained by the editorial design firm.

(6) A publisher has an office in California and an office in New York. The publisher's California office purchases camera-ready art from a California production firm with title passing in California. However, the production firm, on instructions from the publisher, ships the camera-ready art directly to the publisher's New York office for use at the New York office, with no use of the camera-ready art in California.

Tax does not apply to the production firm's gross receipts from the sale of the camera-ready art, because the sale is in interstate commerce.

(7) A commercial artist (such as a commercial photographer or illustrator) makes a temporary transfer of finished art (such as a photograph or illustration) that qualifies as a technology transfer agreement under subdivision (b)(2)(D)2. of Regulation 1540 to a publisher for purposes of reproducing the finished art in a children's book. The publisher makes a computer scan of the finished art and returns the original finished art to the commercial artist. The publisher incorporates the computer scan into layouts which are used to reproduce the finished art in the printed children's books, which are then sold. The commercial artist is paid an advance against royalties, and is then paid royalties based on retail sales of the children's book. The commercial artist does not make a separate charge for the tangible personal property leased to the publisher in accordance with subdivision (b)(2)(D)2.a. of Regulation 1540. As provided in subdivision (b)(2)(D)2.b. of Regulation 1540, if the commercial artist has leased like property for a separate price to an unrelated third party without also transferring an interest in the copyright, or has leased that finished art or like finished art for a separate price satisfying the requirements of subdivision (b)(2)(D)2.a. of Regulation 1540, then tax applies to that separate price. Otherwise, tax applies to the commercial artist's transfer as specified in subdivision (b)(2)(D)2.c. of Regulation 1540. Except for the tax due under subdivision (b)(2)(D)2.b. or (b)(2)(D)2.c. of Regulation 1540, no further tax is due on the royalties or the advance paid to the commercial artist. Tax applies to the retail sales of the children's book unless specifically exempt by statute.

Regulation 1528. PHOTOGRAPHERS, PHOTOCOPIERS, PHOTO FINISHERS AND X-RAY LABORATORIES.

Reference: Sections 6006, 6009, 6015, and 6020, Revenue and Taxation Code.

(a) PHOTOGRAPHERS AND PHOTOCOPIERS. Tax applies to sales of photographs, whether or not produced to the special order of the customer. Tax applies to sales of photocopies, whether or not produced to the special order of the customer, and to charges for the making of photographs or photocopies out of materials furnished by the customer or others. Except as provided in subdivision (b)(2), no deduction is allowable on account of expenses such as travel time, telephone calls, rental of equipment, or salaries or wages paid to assistants or models, whether or not such expenses are itemized in billings to customers.

Tax does not apply to sales to photographers and persons who make photocopies of tangible personal property which becomes an ingredient or component part of photographs or photocopies sold, such as mounts, frames, sensitized paper, and toner but does apply to sales to the photographer or producer of materials used in the process of making the photographs or photocopies and not becoming an ingredient or component part thereof, such as chemicals, trays, films, plates, proof paper, cameras, and copy machine drums.

See Regulation 1540, *Advertising Agencies and Commercial Artists*, for transfers of photographic images by commercial artists.

(b) PHOTOCOPYING OF RECORDS.

(1) GENERAL RULES. Tax applies to sales of photocopies of records. Persons who make and sell, or obtain and sell, photocopies of records to consumers are retailers of the photocopies whether they make the photocopies themselves, hire a subcontractor to make the photocopies, or acquire the photocopies for resale from the person who owns or maintains the records. Tax applies whether or not the copies are made at the business location of the retailer or at the location of the person who owns or maintains the records. The tax applies to the entire charge for making and selling, or obtaining and selling, photocopies, without deduction for expenses incurred in obtaining access to the records, travel time, time spent in selecting the particular records desired, the field service of photocopying or microfilming the records, telephone calls, file setup charges, basic fees, typing fees, document handling fees, or any other costs or expenses of filling the customer's order.

(2) SERVICE TRANSACTIONS. Merely because a fee is charged in connection with the transfer of a photocopy of a record does not mean that the transaction is a sale transaction under the Sales and Use Tax Law. If a person who owns or maintains the records (recordholder) is required by law to furnish the photocopy upon tender and payment of a fee, the transfer of the photocopies by that person is not a sale. For sales and use tax purposes, that person is the consumer of the photocopies transferred and charges by a photocopy company to the recordholder for the photocopies are subject to tax.

(A) Medical Records. Ordinarily tax does not apply to charges made by a hospital or other health care provider (recordholder) for photocopying of medical records. The transaction is regarded as a service transaction, and the fees are nontaxable if the photocopies are furnished to the patient, or to someone acting on behalf of the patient, or to the patient's representative as provided in Health and Safety Code section 123110(b). Likewise, the fees are nontaxable if the photocopies are furnished in response to a written authorization presented by an attorney or the attorney's representative as provided in Evidence Code section 1158, or if the photocopies are furnished as provided in subdivision (b)(2)(C) below. Tax does apply, however, if the hospital or other health care provider is not required by law to furnish photocopies but otherwise sells photocopies of records for a price. Charges made by a photocopy company directly to the requesting party for photocopies which, by agreement with the recordholder, were made and furnished directly to the requesting party are taxable in their entirety.

The preparation and service of a written authorization as provided in California Evidence Code Section 1158 is a nontaxable service. The tax does not apply to separately stated charges for this service even though the written authorization is served in connection with the performance of a contract to produce and deliver photocopies of records.

(B) Public Records. Tax does not apply to charges made by a public agency for photocopies of records furnished pursuant to the California Public Records Act or local law, ordinance, or resolution. Persons who obtain photocopies of public records from public agencies and sell the photocopies are making retail sales and must pay sales tax measured by their entire charge, including reimbursement of legally required fees.

(C) Witness Fees. Copying, witness, mileage or other fees which are charged by a person who furnishes copies of records in response to a subpoena as provided in California Evidence Code Section 1563 are not subject to tax. Separately stated charges by a photocopy company for the reimbursement of witness fees which were paid to the recordholder are not subject to tax. Tax does not apply to separately stated fees, made by a person who makes or acquires records for another for advancing payment of statutory witness fees. Such fees, commonly identified as "check charges", are made to cover the cost of providing the check, advancing moneys, and associated bookkeeping costs. When a witness fee is charged, the "check charge" will be regarded as part of the charge for a nontaxable service and not as a part of the charge made for the tangible personal property.

(3) PREPARATION OF SUBPOENA DUCES TECUM. The preparation and service of a subpoena duces tecum is a nontaxable service. The tax does not apply to separately stated charges made for the service even though the subpoena is served in connection with the performance of a contract to produce and deliver photocopies of records.

(4) TYPEWRITTEN TRANSCRIPTIONS AND INTERPRETATION OF MEDICAL RECORDS. The tax does not apply to a separately stated charge made for providing a typewritten transcription of a medical report or an interpretation of the contents of a medical

record. However, the tax applies to the fair retail value of any photocopies produced for the customer in connection with the nontaxable service.

(c) PHOTO FINISHERS.

(1) **PRINTS AND ENLARGEMENTS.** Tax applies to charges for printing pictures or making enlargements from negatives or slides furnished by the customer.

Tax applies to sales to photo finishers of all tangible personal property used by them in printing pictures or making enlargements except property becoming an ingredient or component part of the prints, enlargements and other items sold by them.

(2) **COLORING AND TINTING.** Tax applies to charges for coloring and tinting new pictures.

Tax does not apply to sales of colors and tints to photo finishers for use by them in coloring and tinting new pictures.

(3) **FILM PROCESSING.**

(A) Negative Development of Customer Furnished Film. Tax does not apply to separately stated charges for the negative development of customer furnished film. Development of film by the reverse process method is not the negative development of film.

Tax applies to sales of chemicals for use in such negative development whether or not the chemicals become a component part of the negative.

(B) Other Film Processing. Tax applies to all film processing charges other than separately stated charges for the negative development of customer furnished film. For example, tax applies to charges for development of film by the reverse process method.

Tax applies to sales of chemicals for use in such film processing if the chemicals do not become a component part of the processed film transferred to customers. Tax does not apply to sales of chemicals which do become a component part of film sold to customers before use.

(d) X-RAY LABORATORIES. Producers of X-Ray films or photographs for the purpose of diagnosing medical or dental conditions of humans, excluding such films and photographs used only for cosmetic purposes, are the consumers of materials and supplies used in the production thereof. Thus, the tax applies to the sale of such materials and supplies to laboratories producing X-Ray films or photographs for the purpose of such diagnoses. Whether the laboratory is a "lay laboratory" or is operated by a physician, surgeon, dentist or hospital is immaterial. Producers of X-Ray films or photographs for any other purpose such as use for purely cosmetic purposes, diagnosis of medical or dental conditions of animals, inspection of metals, welds and similar purposes are retailers of the films or pictures and the tax applies to the gross receipts from the retail sale thereof. If, however, an X-Ray laboratory contracts to furnish an X-Ray inspection

service, retaining title to and possession of the X-Ray or pictures produced, charges for the performance of such an inspection service are not subject to tax.

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Regulation 1540

Regulation 1540, *Advertising Agencies, Commercial Artists and Designers*, is the successor to Board of Equalization Ruling No. 1 (effective 1933), and Ruling No. 2 (an amendment of Ruling No. 1, effective 1950). Ruling No. 2 was renumbered as Regulation 1540 in 1971. The current form of the regulation, Exhibit 2, results from extensive amendments in 1999 (effective April 23, 2000). The regulation interprets, implements, and makes specific RTC sections 6006 through 6015 involving transactions by advertising agencies, commercial artists and designers.

The basic framework of Regulation 1540 was established by Ruling No. 2. In this ruling, the Board recognized that the activities of advertising agencies could include both taxable and nontaxable transactions and that advertising agencies sometimes acted as agents of their clients when making purchases from third-party vendors. If an advertising agency qualified as an agent, a purchase on behalf of its client was regarded as a retail sale by the vendor to the client and tax applied to the vendor's gross receipts. If the advertising agency did not qualify as an agent, the advertising agency was purchasing the property for resale and tax applied to the advertising agency's retail sale measured by the total amount the advertising agency received from that sale of tangible personal property to its client. The ruling also provided general guidelines for determining agent status. These included the nature of the contract, the conduct of the parties involved, and the facts and circumstances of the transaction. Ruling No. 2 also provided that charges for art produced for the purpose of visualizing an idea were not taxable. However, it specifically stated that tax applied to charges for artwork sold for reproduction or display.

A 1961 amendment to Ruling No. 2 added detail on the application of tax to the various charges or services of an advertising agency:

- Services unconnected with a sale of tangible personal property were not taxable. Examples included the writing of original manuscripts, news releases, or advertising copy, and the placement or delivery of advertising. Charges for services in support of nontaxable activities were not taxable. Support included supervision, consultation, research, and travel expenses.
- Commissions or fees charged in connection with nontaxable services were not taxable.
- Tax applied to the entire charge for tangible personal property sold to clients.

The amendment also introduced the concept of "preliminary art" which it defined as "roughs, visualizations, comprehensives or layouts prepared for acceptance by clients before a contract is entered into or approval is given for finished art." The amendment provided that separately stated charges for preliminary art were not taxable unless the art was incorporated into finished art. Separately stated charges had to be clearly identified on the billing as being for preliminary art. Proof of ordering the final art was to be evidenced by purchase orders of the buyer, or work orders or other records of the seller. "Finished art" was defined as the final art used for reproduction by photomechanical or other processes.

Ruling No. 2 was renumbered as Regulation 1540 in 1971, and the regulation was substantively amended concerning: 1) “agent” status and its effect on the application of tax, and 2) the application of tax to services rendered by advertising agencies in connection with sales of tangible personal property. The amendments in 1974 defined an agent as one who represents a principal in dealings with third persons. An advertising agency may either act as an agent for its clients or it may act on its own behalf. If it qualifies as an agent, an advertising agency is neither a purchaser nor a seller of property purchased on behalf of its clients and the advertising agency’s charge to the client for the property is not taxable. If it is acting on its own behalf, the advertising agency is a consumer of items purchased for use, and the agency is a retailer of the tangible personal property purchased for resale, except when the property is purchased by the agency’s client for resale.

To establish its agent status, an advertising agency must: 1) clearly disclose to the supplier the name of its client; 2) obtain and retain written evidence of agent status prior to the acquisition; and 3) bill the client the same amount that was paid to the supplier. In addition, the advertising agency must make no use of the property for its own account and should separately invoice its client for the reimbursement. Advertising agencies making purchases on behalf of clients should not issue resale certificates for purchases.

Even if the advertising agency qualifies as an agent for some purchases, it is still considered a retailer of items produced or fabricated by its employees in-house. Consequently, it is not an agent in regard to materials acquired for incorporation into property prepared by its employees.

The 1974 amendments recognized that client billings may include the selling price of tangible personal property as well as compensation for expenses and services related to the production of the property, and provided that tax applies to the total amount of a retail sale whether the property is acquired from an outside source or is prepared by an employee. The revision also lists specific types of charges that are taxable. These charges include labor or service costs for the production of the property, supervision, consultation, research, postage, model or talent fees, typography or other services involved in the production, and telephone or travel expenses.

If an advertising agency includes the selling price of the property in a combined charge that includes other nontaxable charges, tax applies to the “fair retail selling price” of the tangible personal property sold, defined as: 1) the net labor costs of the employees plus an allowance for overhead and profit of not less than 100 percent of the labor cost, plus 2) cost of the purchased items incorporated into the property. Firm quotes based on these criteria are considered a fair retail selling price.

The 1974 amendments to Regulation 1540 also provided that tax does not apply to any charge an advertising agency incurs in connection with nontaxable activities on behalf of its clients. This includes fees and commissions for nontaxable activities. However, a general fee added to a billing with both taxable and nontaxable activities is taxable in accordance with the ratio of the taxable and nontaxable charges.

The 1974 amendments did not change the rules governing preliminary art or purchases of supply items that were established in previous versions of the regulation.

Amendments subsequent to 1974 include:

- An amendment in 1976 provided that advertising agencies, artists, or designers are consumers of art or photographs used to prepare tangible personal property for resale. If art or photographs are physically incorporated into the work, they may be purchased for resale. Mere use of an image is not physical incorporation.
- An amendment in 1983 clarified when a resale certificate may be issued to a supplier. This amendment explains that a person purchasing tangible personal property as an agent of its client would not be purchasing the property for resale and thus may not issue a resale certificate to the supplier. If a certificate is issued, it is presumed that the agency is buying on its own behalf for resale and not as an agent.
- An amendment in 1994 detailed the documentation required of commercial artists, designers, or advertising agencies who produce preliminary artwork on data processing equipment. As provided, they must produce a hard copy of claimed preliminary art and retain the copy as part of their books and records.

Effective April 23, 2000, the following amendments to Regulation 1540 were made:

- Excluded from tax charges for preliminary art services unless title or permanent possession of tangible personal property is passed to the client by contract.
- Provided a rebuttable presumption that an advertising agency is acting as an agent in acquiring tangible personal property for its client except for items produced in-house.
- Established a presumption that when a lump-sum charge includes the charge for artwork and specified conceptual and design services, 75% of the lump-sum charge is for nontaxable conceptual and design services.
- Established the method to calculate the taxable selling price of tangible personal property when an advertising agency, graphic artist, or designer makes a lump-sum charge for the retail sale of tangible personal property and nontaxable services.
- Provided that tax does not apply to the sale of an additional license or copyright for purposes of reproduction or to the receipt of royalties for the exploitation of a copyright when the sale of the copyright or receipt of royalties occurs more than one year after the original transfer of artwork or physical media.

It should be noted that since its inception as Ruling No. 2, Regulation 1540 has had two constants. First, it has recognized that advertising agencies could act as either agents of their clients or as retailers with respect to tangible personal property acquired from third-party vendors. The regulation has consistently specified that when acting as a retailer, tax is due on the total amount received from the client. Second, concept development, which usually includes the production of art for the purpose of visualization and approval of that concept (preliminary art), has been recognized as a nontaxable service, but the regulation has consistently provided that charges for art sold for reproduction or display are subject to tax.

Amendments to the regulation have served to define and refine the application of tax to the activities of advertising agencies and commercial artists.

Regulation 1541

Regulation 1541, *Printing and Related Arts*, previously Ruling 24 effective in 1939, interprets and explains the application of tax to sales of tangible personal property to and by printers. The regulation interprets, implements, and makes specific RTC sections 6006 through 6012. In 1971, Ruling 24 was renumbered to Regulation 1541.

The regulation was substantially amended in 1972. One of the amendments provided a definition of “special printing aids.” The definition for special printing aids included aids that are of unique utility to a particular customer and that are reusable. The definition also specifically excluded printing plates that were designed for one time use. A standard of proof was incorporated that would allow special printing aids to be deemed sold prior to use if the special printing aids were separately listed and priced from the printed matter on the sales invoice. Without such a listing, an explicit agreement in writing of title transfer between the buyer and seller would have to be present. Clarification on illustrations was also provided. The transfers of photographs, drawings, paintings, handlettering, and other artwork were considered subject to tax. Transfers of photographic reproductions were also considered taxable.

In 1999, amendments to Regulation 1541 provided the following:

- With respect to sales of printed material that is “ultimately subject to sales tax,” a presumption that the selling price of the printed material includes the selling price of special printing aids.
- That charges for alterations of filmwork for \$100 or less constitutes nontaxable repair, while charges over \$100 are taxable fabrication.
- That otherwise qualifying typography remains typography when “clip art” is combined with text on the same page.

Regulation 1543

Regulation 1543, *Publishers*, was developed in cooperation with the publishing industry. In 1988, Bookbuilders West, a publishing industry association, petitioned the Board of Equalization for the adoption of a sales and use tax regulation for the publishing industry. Regulation 1543 became effective March 17, 1991. It interprets and explains the Sales and Use Tax Law as it applies to the sales and purchases of tangible personal property by publishers of printed literature. The regulation defines terms that are peculiar to the publishing industry and provides guidance in the application of tax to the activities of the publishing industry.

In December 1991, the regulation was amended to reflect the repeal of the exemption for the sale of newspapers and periodicals and for the sale of a photograph when the possession, but not the title, was transferred for the purpose of being reproduced one time only in a newspaper. This amendment was a result of the repeal of the newspaper and periodical exemption under RTC section 6362 effective July 15, 1991.

In 1996, the regulation was amended to include columns, cartoons, or cartoon strip drawings in the definition of “manuscripts,” and to treat transfers of such items to syndicators the same as transfers of original manuscripts (or copies thereof) from authors to publishers (that is, as a transfer incidental to the providing of a nontaxable service).